

UNIVERSITY OF CAPE TOWN

Faculty of Law - School for Advanced Legal Studies

Towards a more flexible structure of the share capital

*A comparison of the company law of South Africa and Switzerland with regard
to current debates and developments in the EU*

Katja Fuchs Mtwebana

FCHKAT001

(Contact telephone number: 0941 / 79'252'78'18)

Supervisor: Prof. Richard D. Jooste

Cape Town

2005

Research dissertation presented for the approval of Senate in fulfilment of part of the requirements for the degree of Master of Laws in approved courses and a minor dissertation. The other part of the requirement for this qualification was the completion of a programme of courses.

I hereby declare that I have read and understood the regulations governing the submission of Master of Laws dissertations, including those relating to length and plagiarism, as contained in the rules of this University, and that this dissertation conforms to those regulations.

Signature

A Outline

South Africa reformed its company law significantly with the Companies Amendment Act in 1999 and introduced a modern approach in relation to the share capital with the abolishment of the capital maintenance rule. South Africa followed thereby partly the examples of the American Revised Model Business Corporation Act, the Canada Business Corporations Act and the New Zealand Companies Act. But contrary to the American and New Zealand model South Africa retained the share capital accounts, the share capital account in respect of par value shares and the stated capital account in respect of no par value shares. The striking alteration relative to the abolishment of the capital maintenance rule is that a company may now make payments to its shareholders out of its capital funds without a reduction of its share capital.

Switzerland on the other hand is still ruled by capital maintenance principles. Every stock corporation must dispose of a minimal share capital when founded and may not make payments out of it to its shareholders during its existence unless a capital reduction obeying a strict formal procedure has been carried out. Furthermore share capital must be divided into par value shares with a minimum value of 1 cent each; shares of no par value are not allowed. This formalistic approach towards the capital structure has lately been put into question by several important law authorities within the country. It has been questioned whether this rigid system is really appropriate to meet the actual economic and social challenges company law is nowadays confronted with. Even though these renowned authors agree that a more flexible structure of the share capital is desirable and would render Swiss company law more attractive and competitive the proposed reforms are far from being uniform. Different models have been discussed from the most advanced proposal closely following the principles of the American Revised Model Business Corporation Act to far more moderate suggestions concerning basically the introduction of the so called 'notional no par value shares'. The engine behind these discussions is to be seen in the current reform ambitions in respect of Swiss Company Law.

The company law situation within the member countries of the European Union - of which Switzerland is not yet part of - is shaped and constrained by the framework provided by European Company Law. As concerns the topic of this assignment the Second Company Law Directive of 13 December 1976 is of importance as it contains minimum standards in relation to the share capital of public companies. It clearly upholds the capital maintenance rule through different provisions for example, the prohibition of the issuing of shares at a price lower than their nominal value or, where there is no nominal value, their 'accountable par' or the prohibition of advancing funds, making loans or providing security with a view to the acquisition of its shares by a third party. There are numerous additional provisions throughout the directive which let assume that a company's shares must have either a nominal value or an accountable par. There are ambitions within the European Union to simplify the Second Directive as part of its on-going deregulatory 'SLIM' (Simpler Legislation for the Internal Market) initiative. Furthermore a fundamental review of the capital maintenance regime is envisaged by the European Commission. These efforts could eventually lead to a relaxation of the capital maintenance rule or even to a replacement of the present regime.

In this assignment the current legal situation of South Africa and Switzerland with regard to the share capital structure will be examined as well as the movements within both countries towards a more flexible capital structure. This will be followed by a preview on probable future reform steps. Thereby the developments in Switzerland cannot be analyzed completely independent of the developments anticipated within the European Union. Finally a valuation will take place whether South African Company Law can serve as role model for Swiss Company Law and whether the American Revised Model Business Corporation Act still provides the basis for further developments in South Africa.

B Table of contents

1. Legal situation in South Africa	4
1.1. The evolution of South African Company Law	4
1.2. Capital maintenance rule before 1999	6
1.2.1. Origin of the rule	6
1.2.2. Content of the rule	6
1.2.3. Aim of the rule	7
1.2.4. Prohibition of dividends out of share capital	9
1.2.5. Prohibition of a repurchase by a company of its own shares	10
1.2.6. No issue of shares at a discount	12
1.2.7. No financial assistance by a company for the purchase of its shares	13
1.2.8. Criticism on the rule	14
1.3. Abolishment of the capital maintenance rule	16
1.4. Achievements of the Companies Amendment Act 1999	20
1.4.1. In General	20
1.4.2. Acquisition of own shares	21
1.4.3. Payment of dividends	22
1.4.4. Financial assistance for the purchase or subscription of own shares	22
1.5. Criticism on the Companies Amendment Act 1999	23
1.6. Reform steps to be expected	31
2. Legal situation in Switzerland	37
2.1. Capital maintenance rule	37
2.1.1. Introduction	37
2.1.2. The Raise of Share Capital (Principle of Coverage)	39
2.1.3. Maintenance of Capital	40
(a) Distributions to shareholders	40
(b) Legal reserves and reserves according to the articles of incorporation	41
(c) Acquisition of own shares	42
(d) Financial assistance to purchase shares	43
(e) Share capital reduction	44
2.1.4. Signal for emergency measures	45
2.2. Criticism on the share capital concept	46
2.3. Schemes for a more flexible share capital structure	51
2.4. Valuation of the discussed schemes	57
2.5. Reform steps undertaken	61
2.6. Reform steps to be expected	63
3. Legal situation in EU	65
3.1. Capital maintenance rule	65
3.2. Reform steps to be expected (short term)	67
3.3. Reform steps to be expected (medium term)	69
3.4. Excursus: Legal situation in GB	71
4. South Africa: a role model for Switzerland?	74
5. Revised Model Business Corporation Act: a role model for South Africa?	76
6. Summary	78

1. Legal situation in South Africa

1.1. *The evolution of South African Company Law*

Like other members or former members of the British Commonwealth South Africa shares the legal heritage of English company law which it followed most closely for more than a century.¹ Until the 1960's the initiative for change in matters of company law reform usually came from England and *"after reforms had been put in place there, other commonwealth countries followed later with legislation which was broadly similar"*². The first company legislation in South Africa, the Joint Stock Companies Limited Liability Act 23 of 1861 of the Cape was almost identical to the English Limited Liability Act 1855.³ Other states and colonies within South Africa followed this example and after the Union the first South African Companies Act in 1926 was also completely based on its English predecessor. Later amendments generally followed the modifications previously undertaken in the English company legislation. English case law was therefore very important when interpreting the South African Companies Act and was treated as 'persuasive authority' of great weight⁴ especially in cases where no guidance could be found in South African common law.⁵ As far as the presently interesting capital maintenance rule is concerned, its origin is to be found in English common law and was subsequently accepted by South African courts with little modification.

The enquiry into the Companies Act 1926 by the Van Wyk de Vries Commission and its reports between 1970 and 1972 eventually brought a new approach to the reformation process of South African Company Law. For the first time South

¹ JSE Fourie 'South African Corporate Law Reform - Lessons from abroad' in JJ Henning/PA Delpont/MM Katz (eds) *Selected Essays on South African Entrepreneurial Law* (Bloemfontein: University of the Orange Free State Coordinating Research Institute for Corporate Law, 1996) 62.

² LS Sealy 'Corporate Law Reform: The Commonwealth Experience' in JJ Henning/PA Delpont/MM Katz (eds) *The Future Development of South African Corporate Law* (Bloemfontein: University of the Orange Free State Coordinating Research Institute for Corporate Law, 1994) 1 at 2.

³ JT Pretorius/PA Delpont/M Havenga/M Vermaas *Hahlo's South African Company Law through cases* 6ed (Kenwyn, South Africa: Juta & Co., 1999) 2.

⁴ *Partnership in Mining Bpk v Federale Mynbou Bpk* 1984 (1) SA 175 (T); RC Beuthin / SM Luiz *Beuthin's Basic Company Law* 2ed (Durban: Butterworths, 1992) 3.

⁵ HS Cilliers et al *Corporate Law* 3ed (Durban: Lexisnexis Butterworths, 2000) para 2.13-2.14.

Africa did not simply follow the English precedent but tried to find its own solutions where good reasons for doing so could be found. For example the Companies Act of 1973 introduced the system of no par value shares which is unknown to its English predecessor. It has been said that with the enactment of the Companies Act 61 of 1973 South Africa has left the traditional approach and effectively cut 'the umbilical cord' between English and South African company law.⁶ The continuing separation of these legal systems is due to the differing social and economic factors within these two countries.⁷ On the one hand England has become a member country of the EU and is therefore required to incorporate the EC Directives on Company Law into their own Company Law. A harmonization with continental law systems has therefore taken place and consequently an alienation from other common law systems. On the other hand South Africa has become a democratic nation with a new Constitution which asks for absolute supremacy and which has the potential for being a direct source for South African company law.⁸ Decisions of the higher English courts on substantially similar provisions are certainly as well in future to be treated "*with the utmost respect*" and will still have "*persuasive force*"⁹ but, it is an undeniable and irreversible process in South Africa to rather look to other systems of company law which also have their origin in English Company Law but have started to pursue their own legal paths already, a long time ago.¹⁰

As such countries which are closely observed in South Africa with regard to their company-law developments are to be mentioned the United States, Canada, Australia and New Zealand. The importance to pursue attentively the significant trends within these jurisdictions has been recognized and officially confirmed in several press statements by the Standing Advisory Committee on Company Law

⁶ Pretorius et al (note 3) at 2.

⁷ Beuthin/Luiz (note 4) at 4.

⁸ MS Blackman 'Companies' LAWSA vol 4, Part 1 First Reissue (Durban: Butterworths, 1997) para 5.

⁹ Blackman (note 8) at para 3; HR Hahlo/E Kahn *The South African Legal System and its Background* (Cape Town: Juta, 1968) 200.

¹⁰ Sealy (note 2) at 2-3.

(SAC)^{11, 12} Several areas distinguished by the SAC for the development of company law have already undergone significant reforms for example, the capital maintenance rule with the introduction of the solvency and liquidity test in its place, the related possibility of a company to purchase its own shares and many others. Further anticipated developments foremost within the area of share capital are to be considered below section 1.6.

1.2. Capital maintenance rule before 1999

1.2.1. Origin of the rule

The capital maintenance rule originated in Great Britain and was established by one of the landmark cases of company law, the decision of the House of Lords in *Trevor v Whitworth*¹³. Lord Watson formulated the famous passage which was decisive forthwith for the rules governing the maintenance of share capital by a company in common law jurisdictions: *“Paid-up capital may be diminished or lost in the course of the company’s trading: that is a fact which no legislation can prevent; but persons who deal with, and give credit to, a limited company, naturally rely upon the fact that the company is trading with a certain amount of capital already paid, as well as upon the responsibility of its members for the capital remaining at call; and they are entitled to assume that no part of the capital which has been paid into the coffers of the company has subsequently been paid out, except in the legitimate course of its business.”*

1.2.2. Content of the rule

The term ‘capital maintenance rule’ is misleading. First the doctrine does not require that the value of the shareholders’ contribution of assets to the company is preserved in absolute terms nor does it relate to the assets as stated on the

¹¹ The Committee was introduced on recommendation of the van Wyk de Vries Commission. Its task is to survey on a continual basis both the Companies Act as well as the Close Corporations Act, to make recommendations for the amendment of these Acts and to advise Ministers on such matters, cp. Cilliers et al (note 5) at para 2.19.

¹² Cilliers et al (note 5) at para 2.21-2.23. The full text of the press statement of 1985 has been published in 1985 (Feb) *De Rebus*.

¹³ (1887) 12 AppCas 409 (HL) 423-424.

left hand side of the balance sheet.¹⁴ A distribution of assets back to the shareholders is only and insofar restricted as it can not be effected out of profits available for distribution (i.e. the company's cumulated net realized profits).

'Distribution' may thereby contain a wide range of transactions whereby assets are directly or indirectly transferred to shareholders for less than their market value.¹⁵ 'Capital' refers to the issued share capital as can be found on the right hand side of the balance sheet. Going concern, a company must therefore not necessarily maintain its capital but, it must raise the capital it alleges to raise and not return it to its shareholders otherwise than in terms of a formal reduction obeying thereby the procedure prescribed in the Companies Act of 1973.¹⁶ From the principle of capital maintenance a few particular rules have been deducted in common law which will be discussed in more detail below: a company may not purchase its own shares, it may not pay out dividends out of share capital and it may not issue shares at a discount.¹⁷ Furthermore a company is not allowed to become a member of its holding company.¹⁸ In an illustrative interaction between statute and common law these rules were in the following, complemented by legislation or made subject to statutory exceptions when at the same time receiving enhancement and refinement through later decisions by the courts.¹⁹

1.2.3. Aim of the rule

The capital maintenance rule is principally aimed at protecting the creditors.²⁰ As held in *Ex parte Lebowa*²¹ persons who give credit to the company rely upon the issued share capital for payment of their claims. Shareholders should therefore

¹⁴ J Armour 'Share Capital and Creditor Protection: Efficient Rules for a Modern Company Law?' (2000) 63 *MLR* 355 at 365.

¹⁵ Armour (note 14) at 366.

¹⁶ MS Blackman/RD Jooste/GK Everingham *Commentary on the Companies Act* Volume 1 (Wynberg: Juta and Company, 2002) 5_103-5_104; JT Pretorius 'Capital maintenance doctrine in South African Corporate law' available at www.accaglobal.com/publications/studentaccountant/36856 (accessed 22 March 2005).

¹⁷ Pretorius *ibid*.

¹⁸ Blackman/Jooste/Everingham (note 16) at 5_109.

¹⁹ Cilliers et al (note 5) at para 20.02.

²⁰ *Aveling Barford Ltd v Perion Ltd* (1989) BCLC 626 633; Blackman/Jooste/Everingham (note 16) at 5_105.

²¹ *Ex Parte Lebowa Development Corporation Ltd* 1989 3 SA 71 (T) 101-104.

not be allowed to subsequently withdraw their capital investment. Creditors have a right to look at the share capital as a fund out of which they are to be paid.²² Issued share capital has therefore also been characterized as a rigid 'yardstick' or 'guarantee fund' which fixes the minimum value of the net assets that have to be available to discharge any claims against the company before it could be repaid to the shareholders.²³ As already stated in *Trevor v Whitworth* the risk that the capital would be lost in ordinary business activities is one which the creditor had to bear and the company is under no legal obligation to recover the loss it suffered in the course of the company's trading.²⁴ But apart from that, issued share capital could not be paid out except where a formal reduction of share capital had taken place which had normally to be sanctioned by the court.

Since a reduction of share capital was regarded as being potentially detrimental to the interests of the creditors it was strictly regulated in ss 83-90 as originally enacted in the Companies Act 1973.²⁵ A company could, if so authorized by its articles, reduce its capital by special resolution. According to s 83 the company could do so without confirmation of the court provided that the company has no creditors or all its creditors had consented to the reduction and the reduction affected all its shares or any class of shares proportionately. If these conditions were not fulfilled then the general procedure according to s 84 would apply whereby the reduction had to take place by way of a special resolution subject to the confirmation of the court. If a creditor did object to the reduction then the court could dispense with his consent if the company secured the payment of his debt [s 85 (3)]. If the court was satisfied that every creditor entitled to object has consented to the reduction, or that their debts have been discharged or secured, it could make an order confirming the reduction [s 86(2)].

Although the capital maintenance rule was often referred to as a rule of common law for South Africa this is - as the discussed provisions show - not the case. The

²² per Boshoff J in *Cohen NO v Segal* 1970 (3) SA 702 (W) 705-706; Cilliers et al (note 5) at para 20.01 et seq..

²³ Pretorius (note 16).

²⁴ per Lindley LJ in *Verner v General and Commercial Investment Trust* (1894) 2 Ch 239 264-265 (CA).

²⁵ Beuthin/Luiz (note 4) at 107.

rule was in fact deduced from a proper interpretation of statutory legislation.²⁶ As shown, the Companies Act provided for extensive protection for the company's creditors in the case of a reduction of share capital but contained no provision for their protection where capital funds were returned to the shareholders without a reduction of capital. It could be concluded that the Companies Act indeed prohibited such payments.²⁷

Even though the capital maintenance rule was primarily concerned with the protection of the creditors it could as well be construed as protecting shareholders from prejudice resulting from a diminishment of the value of their shares since directors were not allowed to make further distributions of a company's net assets in case they were less than or equal to the amount of its capital accounts.²⁸

In the following it will be dealt with the 'sub rules' deducted from the capital maintenance rule in more detail following the chronology of their historical development.

1.2.4. Prohibition of dividends out of share capital

The first 'sub rule' which was developed out of the capital maintenance rule was the prohibition to pay dividends out of share capital. The principle was first explicitly stated in *Re Exchange Banking Co (Flitcroft's Case)*²⁹ and later confirmed in *Guinness v Land Corporation of Ireland*³⁰. This prohibition relied on the concept of 'capital fund' at which creditors have the right to look at for the satisfaction of their claims and the use of this fund for the payment of dividends would have constituted an unauthorized application of it.³¹ The Guinness case was followed in South Africa in the case *Cohen NO v Segal*³² where judge Boshoff held:

²⁶ Blackman/Jooste/Everingham (note 16) at 5_105.

²⁷ *Verner v General and Commercial Investment Trust* (note 24) at 264; *Redweaver Investments Ltd v Lawrence Field Ltd* (1991) 5 ACSR 438 443 SC (NSW).

²⁸ Pretorius (note 16).

²⁹ (1882) 21 ChD 519 (CA).

³⁰ (1882) 22 ChD 349 (CA) 375-376, 379-381.

³¹ Pretorius (note 16).

³² (note 22) at 705-706.

“The amount of the share capital and the division thereof into shares of fixed amount must also be stated in the memorandum. Such capital is to be devoted to the objects of the company. Whatever has been paid by a member cannot be returned to him and no part of the corpus of the company can be returned to a member so as to take away from the fund to which the creditors have a right to look as that out of which they are to be paid. The capital may be spent or lost in carrying on the business of the company, but it cannot be reduced except in the manner and with the safeguards provided by the statute. ... It follows from all this that a dividend cannot be declared which has the effect of diverting a portion of the corpus of the company to the shareholders. A dividend may thus, generally speaking, only be declared out of profits, and a resolution which declares a dividend to be paid out of the capital of the company is ultra vires the company.”

The common law further requested in consistent interpretation of this principle that no interest could be paid on shares out of capital.³³ To this principle there was a statutory exception introduced in s 79 of the Companies Act where shares were issued in order to finance construction works or the acquisition of a plant which could not produce profits for a lengthy period.

1.2.5. Prohibition of a repurchase by a company of its own shares

The rule according to which a company was not allowed to buy back its own shares was also stated in *Trevor v Whitworth*³⁴ by Lord MacNaghton and was henceforth known as the English Rule³⁵: *“The third point is one of general importance. It raises the question whether it is competent for a company..., on the principle of limited liability, to purchase its own shares when it is authorised by its articles to do so. The consideration of that question, as it appears to me, necessarily involves the broader question whether it is competent for a limited company under any circumstances to invest any portion of its capital in the purchase of a share of its own capital stock, or to return any portion of its capital*

³³ Cilliers et al (note 5) at para 20.07.

³⁴ (note 13).

³⁵ As opposed to the American Rule which was expressed more than fifty years before the English rule and held that a corporation could purchase its own shares subject to certain limitations; cp. A Trichardt/K Organ/J Cilliers ‘The Purchase by a Company of its Own Shares’ 10 *Transactions of the Centre for Business Law UOFS* (1989) 16.

*to any shareholder without following the course which Parliament has prescribed ... they cannot draw on a fund in which others as well as themselves are interested. That, I think, is the law, and that is the good sense of the matter.*³⁶

The rule was followed in South Africa. It was held by J Coetzee in *The Unisec Group Ltd v Sage Holdings Ltd*, that “Since the earliest days of company law it has been firmly recognized that a company cannot buy its own shares for the reasons set forth by Lord HERSCHELL in *Trevor v Whitworth* (1887) 12 AC 409 (HL) at 416 ... The illegality and voidness of such a purchase actually came to be regarded as part of the common law and is so treated in a number of judgements and by text book writers. The prohibition against such acquisition was not even expressly contained in any of the company statutes until some 50 years ago. So fundamental is this principle. Our 1926 Companies Act, which followed the English Companies Act very closely, did not contain any provision expressly prohibiting such purchases and moreover contained no provisions at all relating to subsidiary or holding companies. The employment of a company’s fund in the purchase or, in loans upon security of the company’s shares, was usually dealt with only in the articles but was illegal even in absence of such a prohibiting article. ... This is some indication of how firmly the law has at all times set its face against such activities.”³⁷

A company could therefore not purchase its own shares even though expressly empowered to do so by its memorandum or articles of association. Such a purchase was considered as void and illegal.³⁸ The precautions contained in the capital reduction provisions aimed at the protection of creditors would have made little sense if a company could simply reduce its capital by a repurchase of its shares.

Furthermore it was considered that trafficking of a company in its own shares could prejudice certain shareholders, especially minority shareholders.³⁹ Directors might have used a share buy-back to maintain themselves in control, to

³⁶ *Trevor v Whitworth* (note 13) at 432, 436.

³⁷ 1986 (3) SA 259 (T) 264-265; see also *Sage Holdings Ltd v The Unisec Group Ltd* 1982 (1) SA 337 (W) 347-349.

³⁸ Blackman/Jooste/Everingham (note 16) at 5_41.

³⁹ Trichardt/Organ/Cilliers (note 35) at 98.

manipulate voting power or to buy out inconvenient shareholders.⁴⁰ There would have been no safeguard that the shareholders are treated equitable. Depending on the share price paid, either the remaining or the exiting shareholders could be favored: if a company pays more than the market value of the shares it dilutes the value of the remainder, if it pays too little it increases the value of the remainder and therefore discriminates the selling shareholders.⁴¹ Trafficking in its own shares was therefore considered as being 'ultra vires' the company.⁴² In order to reinforce the prohibition of buying back its shares a company could furthermore not purchase⁴³ its own shares through a subsidiary or nominee company and it could not give financial assistance for the purchase of shares in itself or a holding company.⁴⁴

There were however certain exceptions to the general prohibition of buy-backs:

- a company could redeem redeemable preference shares under s 98 of the Companies Act whereby funds of a fresh issue of shares or profits which would otherwise be available for dividends had to be used;
- a company could be obliged by a court order to repurchase some of its shares by s 252(3) of the Companies Act in case of an oppressive or unfairly prejudicial conduct of it against a shareholder;
- according to certain Acts for example, the Attorneys Act 53 of 1979 a company in terms of s 53(b) of the Companies Act could repurchase its shares because the directors of such companies are - together with the company - jointly and severally liable for its debts.

1.2.6. No issue of shares at a discount

The final sub rule to be developed by courts as an extended interpretation of the capital maintenance rule was the prohibition that shares could be issued at a discount. The rule, established in *Ooregum Gold Mining Co of India Ltd v*

⁴⁰ Trichardt/Organ/Cilliers (note 35) at 10.

⁴¹ LCB Gower *Principles of Modern Company Law* 3ed (London: Stevens & Sons, 1969) 112.

⁴² Trichardt/Organ/Cilliers (note 35) 11.

⁴³ Any allotment, issue or transfer of shares of a company to its subsidiary was void.

⁴⁴ Cp. ss 38 and 39 in their original wording; *Sage Holdings Ltd v Unisec Group Ltd* 1982 (1) SA 337 (W) 348-349; Blackman/Jooste/Everingham (note 16) at 5_41.

*Roper*⁴⁵, was also based on the concept of 'capital fund' on which creditors may rely on. In certain circumstances the issue at a discount is possible according to a statutory exception. In the case of the issue of shares of par value at a discount s 81 of the Companies Act requires thereby the sanction by the court as well as a special resolution by the company whereby the court has a wide discretion whether or not to allow such an issue having regard to all the circumstances of the case. This discretion enables the court to protect the interests of the creditors as well as the interests of the minority shareholders. In relation to the issue of shares of no par value s 82 of the Companies Act requires only a special resolution by the company.

1.2.7. No financial assistance by a company for the purchase of its shares

This prohibition unlike the three other sub rules mentioned above was not developed in common law but was directly introduced as a statutory provision. As usual at that time, the problem was first perceived in England. According to the Greene Committee⁴⁶ the typical situation experienced in practice was that a syndicate agreed to purchase from the existing shareholders sufficient shares to control a company and the therefore necessary money was indirectly provided out of the company's fund. This was considered to be a circumvention of the principle that a company was not allowed to traffic in its own shares. The Greene Committee therefore recommended a statutory prohibition whereby a company was prohibited from providing any financial assistance in connection with the purchase of their own shares by third persons, whether this assistance was granted in form of a loan, a guarantee, a security or by other means. Exceptions to this rule were allowed where the lending of money was part of the company's ordinary business or where it was for a scheme to enable employees to purchase or benefit from shares.

⁴⁵ (1892) AC 125 (HL) 133 and 145.

⁴⁶ Great Britain Company Law Amendment Committee *Greene Report 1925-26* (London: H.M.S.O., 1926) para 30; Cilliers et al (note 5) at para 20.16.

However in 1962 the Jenkins Committee⁴⁷ had its doubt whether the financial assistance by a company for the acquisition of its shares really offended the rule that a company may not buy its own shares since it did not necessarily involve the reduction of the share capital. If the borrower was able for example, to repay the loan then the company's capital remained intact. The justification of the prohibition was rather perceived in the illegitimate risk at the expense of the creditors and minority shareholders which occurred due to the fact that people acquired control of the company by not providing themselves the necessary funds to acquire the shares but rather relied for this object on the funds of the company itself. If the risk of loss materialized then the creditors and minority shareholders would be left with nothing more than a claim against the directors for abuse of their power. Therefore s 54 of the English Companies Act was retained.

The statutory extension *no financial assistance by a company for the purchase of its shares* of the capital maintenance rule was embraced in South Africa in its widest sense with the enactment of s 38⁴⁸ of the Companies Act. The motivation was to ensure that the acquisition of shares is done from the own resources of the acquirer and to prevent the exposure to a possible risk of the company's fund as well as the unauthorized reduction of share capital in certain cases.⁴⁹ The exceptions to this rule are the same as were provided for in English legislation mentioned above.

1.2.8. Criticism on the rule

The capital maintenance rule has been criticized in almost every common law country where it first applied based on the principles developed in English company law. It has been a general perception that the doctrine constitutes an

⁴⁷ Board of Trade, *Company Law Committee Report of the Company Law Committee (Jenkins Report) 1961-62* (London: H.M.S.O., 1962) para 172-173.

⁴⁸ S 38 (1) "No company shall give, whether directly or indirectly, and whether by means of a loan, guarantee, the provision of security or otherwise, any financial assistance for the purpose of or in connection with a purchase or subscription made or to be made by any person of or for any shares of the company, or where the company is a subsidiary company, of its holding company."

⁴⁹ Pretorius (note 16).

imperfect way to protect creditors.⁵⁰ In South Africa the sense of the rule and its sub rules was questioned facing the fact that the South African Companies Act never required a minimum capital amount neither for public nor for private companies.⁵¹ The English company does prescribe a minimum capital complying thereby with the Second EU Company Law Directive of 13 December 1976. In South Africa it has been held that the minimum capital requirements did in any event not correlate with the capital maintenance rule since the rule would do no more than protecting creditors in their trust to the capital actually paid in (no matter how much this might be).⁵² But this objection to the criticism seems to be of rather academic nature as far as involuntary creditors as opposed to consensual creditors are concerned. Involuntary creditors would only be protected by the capital maintenance rule if there was a minimum capital requirement.⁵³

Another point of criticism on the capital maintenance rule as it applied in South Africa was the fact that once the capital fund was diminished or lost due to unfortunate trading of the company it did not have to be replaced out of future profits. This again was unlike the situation in England where past losses had to be adjusted out of profits unless they could be written off in prescribed ways. The major weak point of the capital maintenance rule - out of the perspective of the creditors - was that it was not directed at the question whether the company was really able to pay its debt when they become due (i.e. the solvency of the company) but rather constituted a regulation for payment transactions from and to particular accounts.⁵⁴ It was therefore criticized of doing virtually nothing in respect of the real concerns of creditors.

⁵⁰ Cilliers et al (note 5) at para 20.03.

⁵¹ This is in contrary to the Continental European company laws as well as English company law which have - as far as they are part of the European Union - to comply with the minimum capital requirements provided for in the Second Company Law Directive.

⁵² Blackman/Jooste/Everingham (note 16) at 5_110 fn 1.

⁵³ Armour (note 14) at 368.

⁵⁴ Simplification Task Force Attorney-General's Department Barton ACT 2600 'Corporations Law Simplification Program Share Capital Rules Proposal for Simplification' available at http://www.takeovers.gov.au/content/743/download/share_capital_rules_november_1994.pdf (accessed 20 October 2005) at 2.

A further critical point - but in this case out of the perspective of shareholder value - is that the rigid capital maintenance rendered it difficult for a company to protect itself against manipulation of its share prices.⁵⁵ Even though this argument had been stressed to a lesser degree in South African doctrine and even though it is questionable whether such a back up of share prices might really be desirable it was ultimately this point which was decisive for the rapid preparation and implementation of the amendments in 1999, i.e. the abolishment of the capital maintenance rule.

1.3. *Abolishment of the capital maintenance rule*

The point of origin when discussing the abolishment of the capital maintenance rule in general is always the development during the 1970s in the United States. It became generally recognized in that country that the statutory structure of 'par value' and 'stated capital' did not serve its original purpose in protecting creditors and minority shareholders. According to this doctrine, creditors as well as minority shareholders were able to better regulate their protection through negotiated agreements.⁵⁶ When in 1979 all provisions regarding financial matters were modernized in the Model Business Corporation Act, the concept of stated capital and par value were deleted. This fundamental change in the United States was responsible for boosting the reformation process throughout the landscape of other common law countries.⁵⁷

The reform process in other commonwealth jurisdictions was often initiated by broad based law reform projects or through standing advisory committees established especially for this purpose. In each of the common law jurisdictions concerned (such as Ghana, Ontario, Federal Canada, Jersey and New Zealand)⁵⁸ loads of materials like working papers, reports and commentaries⁵⁹

⁵⁵ Pretorius (note 16).

⁵⁶ Committee on Corporate Laws 'Changes in the Model Business Corporation Act – Amendments to Financial Provisions' (1979) 34 *Bus. Law.* 1867 1867-1868.

⁵⁷ Blackman/Jooste/Everingham (note 16) at 5_111; Department of Trade and Industry, South African Companies Registration Office Notice 724 GG 18868 of 8 May 1998.

⁵⁸ For example the Gower report for Ghana, the Kimber and Lawrence reports for Ontario, the Dickerson report for federal Canada, the Morgan report for Jersey and the New Zealand Law Commissions's reports for Australia.

⁵⁹ Sealy (note 2) at 3-4.

were produced and the reform process was supported by a considerable discussion in the respective corporate legal community.

The reform process in South Africa, however, differed quite considerably from such a proceeding. In respect of the Companies Act 1973⁶⁰ the issue of revising the capital maintenance rule was put on the table several times without actually setting in motion law reform measures. In 1985 the SAC first tried to launch the reform program by releasing a policy statement on the future development of Company Law including the recommendation to abolish the capital maintenance rule. Another press statement in this context was released in 1989 with special emphasis on the possibility by a company to purchase its own shares. The Centre for Business Law (University of Orange Free State) submitted a compilation with the title *The Purchase by a Company of its own Shares: the English rule vs the American rule* in 1989 which was partly utilized by the Department of Trade and Industry (DTI) in 1992 in order to stimulate the reform process.⁶¹ An active involvement of or lively discussion within the concerned legal community was nevertheless not achieved.⁶² In 1992 a sub-committee of the SAC was founded, the Coordinating Research Institute for Corporate Law (CRIC)⁶³, with the main objective to review and modernize South African corporate law comprehensively as previously happened in Australia and New Zealand and several other Common Law jurisdictions. A broad involvement of academics and practitioners was thereby intended. In 1993 a three day international conference on the Future Development of South African Corporate Law, initiated by CRIC, was held in Johannesburg with the participation of some of the most acknowledged authorities for national and international corporate law. Certain conclusions were drawn from this conference, of interest for the present

⁶⁰ As regards the Close Corporation, with the enactment of Close Corporations Act in 1984 the capital maintenance rule was first abandoned in favor of a solvency and liquidity test. In this new form of business companies with no more than ten members - which in general must be natural persons - can establish a cheaper and more flexible business entity.

⁶¹ Cp. Department of Trade and Industry, Companies and Close Corporations Registration Office *Proposals in respect of the purchase by a company of its own shares* (Pretoria: 1992).

⁶² Cp. press release of the Standing Advisory Committee on Company Law (SAC) of 21 August 1992, published in Henning/Delpont/Katz (note 2) at 201-202.

⁶³ The CRIC has its seat at the Centre for Business Law of the University of the Orange Free State.

subject is the predominant opinion that the principle of capital maintenance should be abolished in favor of a 'larger fund-maintenance doctrine', that a minimum required capital was not the answer to the weakness of the capital maintenance rule and that the necessity of the distinction between par and no par value shares should be questioned in favor of the no par value shares.⁶⁴ In 1994 SAC and CRIC launched another Corporate Law Reform Programme with different research areas whereas inter alia a thorough revision of the capital rules should take place with an eventual abandonment of the capital maintenance rule. Despite these serious initiatives no relevant break through could be achieved. No further discussion within the corporate community can be traced during the following period wherefore it is difficult to understand how all of a sudden in 1999 the capital maintenance doctrine was nevertheless abolished to a great extent. It is quite surprising how these 'start-up' activities could have met in such a fundamental change brought by the Companies Amendment Act in 1999. However, in 1998 the DTI announced in the Government Gazette⁶⁵ that there was urgency in introducing the necessary amendments to the companies' legislation with respect to the recognition of modern concepts of capital rules. The DTI acknowledged that there were certain technicalities which have not yet been fully cleared but, that the advice of the SAC according to which a new dispensation concerning the ability of companies to purchase their own shares should not be delayed, was embraced. Even though no relevant public involvement in the reform activities of the SAC can be traced and even though the SAC itself acknowledges in its press release in 1993 that there was no such involvement the DTI refers to an "*engaged considerable public attention over a protracted period*" by which the SAC purportedly shall have been influenced when drafting its amendments of the Companies Act.⁶⁶ Almost overnight the Companies Act 1973 was eventually amended in 1999 so as to provide for a company to acquire its own shares.

⁶⁴ *Reportback of issues raised in group sessions* in Henning/Delport/Katz (note 2) at 182.

⁶⁵ Department of Trade and Industry (note 57).

⁶⁶ Cp. as well Fourie (note 1) at 71 where he states that up to 1996 very few articles have been published in South Africa which would involve a major rethinking of areas of corporate law with a view to their reform.

The motivation behind this hasty implementation of amendments takes more shape when reading the *Memorandum on the Objects of the Companies Amendment Bill, 1999*⁶⁷ (*Memorandum to the Bill*) stated by the Minister of Trade and Industry: *"In this regard it should be pointed out that our financial markets have lately entered into derivative activities on a large scale and the Johannesburg Stock Exchange (JSE) and SAFEX are rapidly becoming more complex and sophisticated. Markets have weakened considerably and this can be attributed to, inter alia, market manipulation by international banks and other speculators with unlimited financial resources. This factor alone poses a fundamental danger to our economy.*

There are inherent dangers in the impact of speculative derivative, futures and currency trading activities which are taking place in virtually all developed investment markets and now also in South Africa. These activities if taking place in an unscrupulous way, can easily suppress the prices of shares on the stock market. South Africa has now become a magnet for profitable trading by these speculators. This has resulted in the decline in value of most leading South African shares. Acquiring control of sound companies through these methods could lead to significant job losses and businesses closing down due to asset stripping and other irregular activities.

One of the accepted and effective defences against this negative action in the international marketplace is the ability of strong companies to repurchase and cancel their own issued shares which levels the playing field in relation to those speculators wishing to reduce the value of a company's shares by indiscriminate market activities. Legislation in most of the EEC, USA and other developed markets permits the repurchase of a company's issued share capital, subject to solvency and liquidity criteria."

Even though the Minister of Trade and Industry asserts in the following that *"allowing a company to acquire its own shares to support the market for its shares, thus also preserving for its shareholders the value of their shares, is but one advantage"* and enumerates certain other benefits which such a purchase of

⁶⁷ B17D-99.

its own shares might as well have⁶⁸ these reasons seem to be of rather incidental nature. One cannot help but assume that the abolishment of the capital maintenance rule was to a far lesser degree motivated by academic criticism than by the economic pressure under which certain important shareholdings might have fallen after international investors have started to participate in the JSE Securities Exchange South Africa (JSE).

Be that as it may, the capital maintenance rule as it applied in South Africa since its beginning was to a large extent abolished by the Companies Amendment Act of 1999. Even though the draftsmanship of the Act received serious criticism after its enactment and undisputedly needs further refinement, this important step of the Legislature in order to abolish the capital maintenance rule was broadly welcomed in South Africa's corporate legal community.⁶⁹

1.4. *Achievements of the Companies Amendment Act 1999*

1.4.1. In General

With the Amendment Act 37 of 1999 a fundamental change of philosophy⁷⁰ has taken place as far as the capital maintenance rule is concerned: the rule was to a large extent abolished and with it the departure from the path of English concepts and principles has continued. The new concepts in the Companies Amendment Act 37 of 1999 are heavily based on Canadian legislation, i.e. the Canada Business Corporations Act 1985. Before South Africa, Australia and New Zealand had already taken the Canadian legislation as a role model whereas Canada itself was influenced by precedents in the United States.⁷¹

However, certain provisions in the Companies Act remained which are - quite unsystematically - still upholding the capital maintenance rule.⁷² Among these provisions is the restriction on the issue of shares at a discount, the payment of

⁶⁸ i.e. facilitating employee share schemes, averting hostile take-overs, providing alternative markets.

⁶⁹ Pretorius (note 16); FHI Cassim 'The New Statutory Provisions On Company Share Repurchases: A Critical Analysis' (1999) 116 SALJ 760.

⁷⁰ Pretorius et al. (note 3) at 121.

⁷¹ Cassim (note 69) at 760; Fourie (note 1) at 79.

⁷² Cilliers et al (note 5) at para 20.04.

interest on share capital and the requirements in respect of redeemable preference shares.⁷³

1.4.2. Acquisition of own shares

As shown below section 1.3. the possibility for companies to acquire their own shares was the principal motivator for the reform process realized in 1999. Therefore ss 85-88 of the Companies Act have to be considered as the corner stone provisions within the amendments. S 85 (1) now allows a company under certain circumstances to acquire its own shares provided that a respective special resolution has been passed to this effect and that the company is authorized thereto by its articles. Shares so acquired by a company are to be cancelled and become authorized shares forthwith [s 85 (8)]. Therefore a reduction of the share capital takes place. The acquisition shall not have as a result that only redeemable preference shares remain [s 86 (9)]. The creditors interests are now protected by the very important requirements in s 85 (4) according to which a company may only acquire shares if there is a reasonable belief that the company is, or would after the acquisition be, able to pay its debts as they fall due in the ordinary course of business (the so called *liquidity test*) and that the consolidated assets of the company would after the acquisition exceed its consolidated liabilities (the so called *solvency test*). If these requirements are not met any creditor who was a creditor at the time of acquisition may apply to the court for an order to compel a shareholder to return the received consideration to the company and the company to reissue the shares to that shareholder [s 86(3)]. According to s 86 (1) directors are jointly and severally liable to the company for any consideration given for the acquisition of the shares in contravention of s 84 (4) which is not yet recovered by the company. According to s 89 a subsidiary company may now acquire a maximum of 10 per cent of the issued shares of its holding company.

⁷³ Pretorius et al (note 3) at 122.

1.4.3. Payment of dividends

In consequence, the dividend regulations as considered below section 1.2.4. above have been amended too. In terms of s 90 of the Companies Act a company may now make distributions to its shareholders in their capacity as shareholders if it is authorized hereto by its articles. S 90 (2) requires - similar to s 85 (4) above - that there must be reasonable grounds for believing that the company is, and after the payment will be, able to pay its debts as they fall due (*liquidity test*), and that the consolidated assets will, after the payment, exceed the consolidated liabilities (*solvency test*). According to s 90 (3) 'payment' is broadly defined: it includes any direct or indirect payment or transfer of money or other property but excludes the acquisition of shares in terms of s 85 of the Companies Act, the redemption of redeemable preference shares in terms of s 98 of the Companies Act, the issue of capitalization shares as well as the acquisition of shares in terms of an order of the court (e.g. s 252 of the Companies Act). Excluded however, is a payment to a shareholder by a different virtue than his shareholding in the company, for example in his capacity as a creditor.⁷⁴ The share premium account and the capital redemption reserve fund are as well available for payments to shareholders subject to the requirements in s 90 of the Companies Act.⁷⁵

1.4.4. Financial assistance for the purchase or subscription of own shares

As already discussed below section 1.2.7. above, a company is according to s 38 of the Companies Act prohibited from giving, "*whether directly or indirectly, and whether by means of a loan, guarantee, the provision of security or otherwise, any financial assistance for the purpose of or in connection with a purchase or subscription made or to be made by any person of or for any shares of the company ...*". Even though the Companies Act now allows under certain conditions the acquisition of its own shares according to ss 85-88, s 38 has not substantially changed. The only amendment is paragraph (d) according to which

⁷⁴ Pretorius (note 16).

⁷⁵ Blackman/Jooste/Everingham (note 16) at 5_113.

financial assistance for the acquisition of shares in a company by the company or its subsidiary in accordance with the provisions of s 85 is exempted from the prohibition. But it is far from clear what this concretely means.⁷⁶ However, s 38 does still not provide for an exemption to provide financial assistance to third parties.⁷⁷ A consequential adjustment of s 38 should have taken place in order to fit in with the new philosophy underlying the provisions s 85-88 and s 90 as discussed above. If the financial assistance is bona fide as well as in the best interests of the company and if it meets the solvency and liquidity tests there seems to be no justification why a company should be prevented from rendering it.⁷⁸

Additionally, s 38 renders it difficult to realize the objectives of the Black Economic Empowerment (BEE) Act, 2003. It constrains BEE consortiums who usually have little access to financial means or assets to provide for security against borrowing since a company cannot lend money to potential BEE partners in order to facilitate them the purchase of shares in the company. BEE transactions would clearly benefit from a relaxation of s 38.⁷⁹

1.5. Criticism on the Companies Amendment Act 1999

Although generally acknowledged in South African legal community that the Companies Amendment Act 1999 was a step in the right direction several features of the Act have been heavily criticized. Criticism can be divided into different categories: (a) the motivation of the Legislature for introducing the acquisition by a company of its own shares has been questioned, (b) the draftsmanship of the amendments has been criticized in general, (c) it has been challenged whether the interests of creditors and minority shareholders are sufficiently protected within the new provisions, (d) it has been further criticized that the abolishment of the capital maintenance rule has not been realized with

⁷⁶ Blackman/Jooste/Everingham (note 16) at 5_67.

⁷⁷ Pretorius et al (note 3) at 125.

⁷⁸ A Trichardt/E Brincker 'Future Development of South African Corporate Law - Capital in Company Law' in Henning/Delport/Katz (note 2) 141 at 151.

⁷⁹ Deney's Reitz Attorneys 'Section 38 - Let it BEE?' *Commercial Update No 12* available at <http://www.deney'sreitz.co.za/publications/pdf/Commercial%20Update%20No.12.pdf> (accessed 20 July 2005).

the necessary consequence throughout the Companies Act, (e) that with the repeal of the former ss 83-90 of the Companies Act companies have lost their general power to reduce share capital and finally that (f) the reform in general could have gone further.

It would go beyond the scope of this assignment to restate every criticism brought forward in connection with the Companies Amendment Act 1999. But in the following, a few interesting issues shall receive more detailed consideration.

(a) As already mentioned, the corner stone of the Companies Amendment Act 1999 are ss 85-88 allowing a company under certain conditions to purchase its own shares. Even though there are widely accepted reasons why a company should be able to acquire its own shares (buy-back) the one primarily accentuated in the Memorandum to the Bill is controversial in contemporary legal literature: *to provide means for market manipulation*.

In a given case where a company tries to support the market price of its shares by a buy-back because it believes that its shares are undervalued, the buy-back has necessarily to be carried out at a premium. If the hypothesis of undervaluation proves to be wrong the remaining shareholders are then adversely affected compared with the selling shareholders. If, however, the assumption proves to be right then wealth is shifted from the shareholders who sell to those who remain in the company. Only the remaining shareholders participate in the anticipated glory future of the company and profit furthermore of a higher dividend return per share due to the diminution of the shares.⁸⁰ Even if share buy-backs are not carried out selectively they have nevertheless a considerable coercive element: shareholders are forced to make a decision whether they sell shares or stay with an increased exposure to the company even though they might prefer to do neither.⁸¹ To sum up, share buy-backs in order to influence the market contain a serious danger that shareholders are treated unequal and unfairly.

⁸⁰ RC Clark *Corporate Law* (Boston Toronto: Little, Brown and Company, 1986) 630.

⁸¹ B McCabe 'The Desirability of a Share Buy-Back Power' (1991) 3 *Bond LR* 115 at 128.

It has been furthermore questioned whether there are not more appropriate means to convince the market that the shares are undervalued than by share buy-backs.⁸² Could not a lack of information be the reason for the undervaluation? Should the management of the company not look for more efficient ways to convey relevant facts to the market? Or could a raise of dividends not better express the confidence of the management in the well-being of the company? It has been satisfactorily shown that markets are not likely to “*systematically and persistently*” undervalue public corporations (‘efficient-markets theory’).⁸³ If the market does not sufficiently reward the information about the allegedly bright future of the company then it is far more likely that the inherently biased management rather than the market - which reflects an interaction between rational buyers and sellers⁸⁴ - has wrongly assessed the performance of the company. If through such an ‘irrational’ repurchase of shares by the company the share prices are raised, this is nothing more than a distortion of the market without any useful economic function. Such an exertion of influence by a company could in fact even amount to a crime in terms of s 40(c) of the Stock Exchanges Control Act 1 of 1985.⁸⁵

(b) In one of the most fundamental critical analysis of the new provisions Cassim claims inter alia that the statute is defective and lacking in technical quality.⁸⁶ Even though he welcomes the flexibility and the simplicity he considers some of the provisions as almost rudimentary. He objects that even though the Companies Amendment Act 1999 is basically built after the Canada Business Corporations Act 1985 its draftsmanship would be far from clear. Object of severe criticism is especially the lack of protection of the interests of creditors and minority shareholders which is considered in more detail right below (c).⁸⁷

⁸² Clark (note 30) at 629.

⁸³ Clark (note 30) at 628-629.

⁸⁴ McCabe (note 31) at 128.

⁸⁵ Blackman/Jooste/Everingham (note 16) at 5_58.

⁸⁶ Cassim (note 69) at 780.

⁸⁷ Cassim (note 69) at 780.

With regards to clarity and efficiency of the provisions, several authors held that instead of the Canada Business Corporations Act 1975, the more recent and comprehensive New Zealand Companies Act of 1993 should have been taken as a role model. The New Zealand Companies Act is itself drawn along the lines of the Canada Business Corporations Act 1975 but, could already build on the experience of its predecessor. The New Zealand Companies Act is widely praised for its attractive, simple language which renders it accessible and functional for its users. The Act has implemented most innovative changes in obeying the principles of high flexibility and a maximum of freedom for business ventures.⁸⁸

(c) Share repurchases by a company in general and selective (targeted) repurchases in special bear the danger that shareholders are not treated equally between them. Directors could favor certain shareholders over others or controlling shareholders could obtain an unfair advantage over minority shareholders.⁸⁹ The potential dangers of share repurchases were clearly recognized in the document 'Proposals in respect of the purchase by a company of its own shares' released by the Department of Trade and Industry in 1992:⁹⁰

"Thus, as regards the distribution of assets, the specters of insider trading and price manipulation are raised and must be guarded against. As regards a reorganization of ownership, the unfair or discriminatory treatment of minority shareholders poses a potential problem area which must also be addressed. In respect of asset distribution, asset stripping and debt avoidance are dangers which must be catered for. It is submitted that it would be safe to grant a company the power to purchase its own shares if the power can be exercised only in ways which will not favour one shareholder over another and which will not prejudice potential investors or creditors."

⁸⁸ JJ Du Plessis 'Enkele Internasionale Maatskappyregtelike Ontwikkelings' (1992) *TSAR* 561 at 576; Fourie (note 1) at 80; JPG Lessing 'Company-law Reform in New Zealand' (1990) 2 *SA Merc LJ* 49 at 58.

⁸⁹ Cp. Department of Trade and Industry (note 61) at 101.

⁹⁰ Cp. Department of Trade and Industry (note 61) at 101.

According to Cassim the provisions in ss 85-88 of the Companies Amendment Act 1999 do not provide sufficient protection against these clearly perceived dangers.⁹¹ Especially the aspect of selective share repurchase would have unsatisfactorily been dealt with in the Companies Amendment Act 1999.⁹² According to Cassim the 'solvency' and 'liquidity' test as provided for in s 85 (4) of the Companies Act should be complemented through the adoption of additional requirements in order to obtain the degree of shareholder and creditor protection previously secured by the now abolished capital maintenance rule.⁹³ The Companies Act 1973 as it stands now foresees no limits as to how many shares can be acquired by a company even though of course the transaction has to be approved by a special resolution.⁹⁴ A restriction in this regard was however part of the draft proposals⁹⁵ as it contained a prohibition to acquire more than 1 per cent of the shares in any month by a company.⁹⁶ Australian law for example, prohibits the acquisition of more than 10% of the shares within a twelve-month period⁹⁷. In addition, the draft proposal provided that a company was prohibited from acquiring its shares if there were reasonable grounds for believing that the 'realizable value of the company's assets would after the payment be less than the aggregate of its liabilities and stated or declared share capital plus reserves'.⁹⁸ S 85(4)(b) of the Companies Act as it stands now deprives the creditors of the protection afforded by such a stipulation that the company's share capital is treated as a liability and furthermore the word 'realizable' value is substituted by the 'consolidated' assets/liabilities which seems not to afford any additional protection for creditors.⁹⁹ In addition, s 85(4)(b) does not provide that an amount sufficient to satisfy the preferential rights of shareholders should be

⁹¹ Cassim (note 69) at 776.

⁹² Cassim (note 69) at 776-777; cp. as well Blackman/Jooste/Everingham (note 16) at 5_90-5_91.

⁹³ Cassim (note 69) at 765.

⁹⁴ The JSE's Listings Rules contain however a restriction in Rule 5.88.

⁹⁵ Department of Trade and Industry (note 57), s 7(2).

⁹⁶ Cp. as well Department of Trade and Industry (note 61) at 114.

⁹⁷ S 206C(1) and s 206D(1) of Corporations Law 1995.

⁹⁸ Department of Trade and Industry (note 57).

⁹⁹ Blackman/Jooste/Everingham (note 16) at 5_70.

added to the liabilities of the company. The interests of the preference shareholders are therefore also undermined.¹⁰⁰

Another further requirement proposed by Cassim could be that the necessary authorization in the company's articles for share buy-backs should be renewed by a special resolution after a certain period in order to remain valid.¹⁰¹ As well a statutory declaration provided by the directors could be implemented, which confirms that the company will be able to pay its debts for a certain period after the date of the repurchase.¹⁰² This declaration could thereupon be supported and reinforced by a report of the auditors of the company that the directors have reasonable grounds for their belief in the solvency or liquidity of the company.¹⁰³

The potential danger of so called 'sweet-heart' repurchases, greenmail and 'going-private' transactions could thus be encountered by such additional restrictions and the interests of creditors as well as minority shareholders could thereby adequately be safeguarded.¹⁰⁴

(d) The major critical point below this category is the fact that the capital maintenance rule has not been abolished in respect of s 38 of the Companies Act 1973. Parts of the critics have already been mentioned below s 1.4.4. above. This "*infamous*"¹⁰⁵ provision still prohibits a company from giving financial assistance for the purchase or acquisition of its own shares and therefore maintains the capital maintenance concept in this regard.¹⁰⁶ The very wide ambit of s 38 has been criticized as likely to hit the innocent but of being futile in preventing the guilty.¹⁰⁷ It would be desirable that the solvency and liquidity test applies also in the case of financial assistance provided however, that sufficient further safeguards for creditors and minority shareholders are implemented.¹⁰⁸

¹⁰⁰ Blackman/Jooste/Everingham (note 16) at 5_70.

¹⁰¹ As provided for in Australian Legislation, ss 206 DA and 206 DB of the Corporations Law 1990, cited in Cassim (note 69) at 766.

¹⁰² Cp. s 173(3) (b) of the English Companies Act 1985, cited in Cassim (note 69) at 766.

¹⁰³ Cp. s 173(5) of the English Companies Act 1985, cited in Cassim (note 69) at 766.

¹⁰⁴ Cassim (note 69) at 774-76.

¹⁰⁵ Pretorius (note 16).

¹⁰⁶ Lessing (note 88) at 56.

¹⁰⁷ LCB Gower *Principles of Modern Company Law* 4ed (London: Stevens & Sons, 1979) 227.

¹⁰⁸ Blackman/Jooste/Everingham (note 16) at 4_58.

According to Cassim such further safeguards could be that the resolution to grant financial assistance is made subject to a special resolution by the members of the company as well as to a statutory declaration of the directors supported by an auditor's certificate that the company remains solvent.¹⁰⁹ The company could further - similarly to s 42(4) of the Business Corporations Act of Alberta 1981 - be required to disclose to its shareholders the identity of the person to whom financial assistance is to be granted as well as the nature and the amount of the financial assistance so given.

(e) As discussed below section 1.2.3. the former ss 83-90 of the Companies Act conferred a general power on the company to reduce its share capital with the consent of its creditors and the confirmation of the court. The new s 90 in fact allows payments to shareholders out of capital funds *without a reduction of share capital*; it does not permit a reduction of share capital.¹¹⁰ For the purposes of s 90 of the Companies Act, s 90(3) excludes an acquisition of shares in terms of s 85, a redemption of redeemable preference shares in terms of s 98 and any acquisition of shares in terms of an order of Court [s 252(3)] from the definition of 'payment'. These ss 85, 98 and 252(3) constitute - with one minor exception - the only remaining possibilities to achieve a share capital reduction.¹¹¹ A general power to reduce share capital does not exist anymore.

It is likely that this constraint of a company's power is the result of an oversight of the legislator. One indication for this assumption is the fact that in the model set of Articles for a public company having a share capital (Table A) as well as in the model set of Articles for a private company having a share capital (Table B) the general possibility of a company to reduce its share capital, its stated capital, any capital redemption fund or any share premium account by special resolution is still provided for in TA 31(g) and TB 30(g). Furthermore, the reduction of share capital served to 'decapitalise' part of the capital fund - accompanied or not by the return of the funds to the shareholders. Since the introduction of the new s 90

¹⁰⁹ Cassim (note 69) at 779.

¹¹⁰ Blackman/Jooste/Everingham (note 16) at 5_112.

¹¹¹ Blackman/Jooste/Everingham (note 16) at 5_14.

it is indeed no longer necessary to 'decapitalise' first capital funds by way of a capital reduction before distributions can be made to shareholders¹¹² wherefore the legislator has presumably considered it unnecessary to maintain a general possibility for companies to reduce their share capital. But a capital reduction entails as well an alteration or abrogation of the rights of the shareholders irrespective of whether or not the company actually pays out the 'decapitalised' funds. This is of course foremost the case where shares are cancelled but as well where the par value of shares is reduced or - in the case of no par value shares - where the stated capital account is reduced.¹¹³ And these options to influence the shareholders rights are now no longer available for a company. Especially a compulsory cancellation of shares in order to freeze out a shareholder is not possible anymore via a capital reduction¹¹⁴: the remaining ways for a company to reduce share capital (share buy-backs and the redemption of redeemable preference shares) require both - even though at a different point in time of the transaction - the consent of the concerned shareholders.¹¹⁵ There seems to be no logic explanation for such a reduction in a company's power within a reform process which was generally aimed at rendering the share capital structure more flexible.

(f) Unlike the American Revised Model Business Corporation Act and the New Zealand Companies Act the concept of share or stated capital and nominal capital has not yet been abandoned in the Companies Act 1973. Under those two modern Acts the concept of 'par value', the authorized capital and the issued capital have been given up and shares can be issued in any number, with any conditions and at any (fair) price.¹¹⁶ All distributions by a company are made subject only to liquidity and solvency tests.¹¹⁷ It has been questioned why capital

¹¹² Blackman/Jooste/Everingham (note 16) at 5_112.

¹¹³ Blackman/Jooste/Everingham (note 16) at 5_16.

¹¹⁴ Freezeouts can however still be achieved by converting ordinary shares into redeemable preference shares; cp. Blackman/Jooste/Everingham (note 16) at 5_16.

¹¹⁵ Blackman/Jooste/Everingham (note 16) at 5_15.

¹¹⁶ PA Delpont 'Capital Rules in South African Company Law' in JJ Henning/PA Delpont/MM Katz (note 2) 133 at 139.

¹¹⁷ Blackman/Jooste/Everingham (note 16) at 5_115.

accounts have been retained in South Africa. The only meaning they seem to have after the capital maintenance rule has principally been abolished, is between the shareholders themselves with regard to their claims for surplus assets in the case of a winding-up. In such a case a shareholder has a right to the sum he originally paid for the company's shares before any further distribution of surplus assets is made. The capital accounts serve now simply as a record of the number of par value shares issued, the par value of each share, the total par value and the different classes of issued shares. But there seems to be no reason why such a record should be held in capital accounts.¹¹⁸

The concepts 'nominal capital' and 'par value' have been held as 'arbitrary and misleading' in modern company law systems. This view has also been adopted by Delport for South Africa and he recommended to abolish altogether the distinction between par and no par value shares in favor of no par value shares.¹¹⁹ To support this point of view it has been referred to the famous statement of Dickerson, Howard and Getz that *"A share is simply a proportionate interest in the net worth of a business. Par values obscure this reality, while the concept of a share without par value precisely embodies it... What matters to an investor is the proportionate size of his investment in the corporation, not the arbitrary monetary denomination attributed to that investment"*¹²⁰.

1.6. Reform steps to be expected

In May 2004 the DTI released its Guidelines for a Corporate Law Reform (Guidelines).¹²¹ It points out repeatedly how important and overdue this reform is. It does not tire to emphasize that since the investigation of the Van Wyk De Vries Commission which resulted in the Companies Act 1973, no significant review has taken place but that this time reform shall be of fundamental nature.¹²² The

¹¹⁸ Blackman/Jooste/Everingham (note 16) at 5_16.

¹¹⁹ Delport (note 116) at 139-140.

¹²⁰ RWV Dickerson/JL Howard/L Getz *Proposals for a New Business Corporations Law for Canada* (Ottawa: Information Canada, 1971) 36.

¹²¹ Department of Trade and Industry 'South African Company Law for the 21st Century Guidelines for Corporate Law Reform' (May 2004) available at https://www.saica.co.za/documents/Draft_policy_document_on_Corporate_Law_Reform.pdf (accessed 27 July 2005).

¹²² Department of Trade and Industry (note 121) at 4, 8, 10, 12, 13-14, 20.

capital rules are thereby singled out as one of the major issues to be taken care of during this reform.¹²³ Even though the Companies Act 1973 was praised for loosening its ties with the English law, according to the DTI it remains nevertheless attached to foundations laid down in Victorian England in the middle of the 19th century. According to these Guidelines, the most significant departure from English law was the adoption of the Close Corporations Act in 1984.¹²⁴ Strange enough, in the whole document the Companies Amendment Act 1999 does not seem worthy of being mentioned even with a single word. It is true that this amendment was not preceded - as it was in other countries like Botswana, Hong Kong, Australia, Canada or New Zealand - by an extensive review of a reform committee or a major discussion in doctrine let alone the rest of the corporate legal world. But the Companies Amendment Act 1999 brought nevertheless significant changes especially as far as the capital rules are concerned. The Guidelines give the erroneous impression that the capital maintenance rule is in principle still upheld in the Companies Act 1973 which is clearly not the case. In its disregard of the changes introduced in 1999 the policy paper even recommends an investigation whether the US style 'solvency-liquidity test' with no initial paid up capital should apply as well for South Africa.¹²⁵ Given the fact that an almost identical test¹²⁶ already applies for share repurchases according to s 85 (4) of the Companies Act and distributions to shareholders according to s 90 (2) of the Companies Act and that furthermore South African Company Law never knew a minimum capital requirement these considerations seem somehow bizarre. The abolishment of the capital maintenance rule in 1999 might not have been executed with every desirable consequence but it was unquestionably a serious step in adopting modern capital rules. It could not have been the intention of the Companies Amendment Act 1999 to adopt a middle

¹²³ Department of Trade and Industry (note 121) at 20.

¹²⁴ Department of Trade and Industry (note 121) at 13.

¹²⁵ Department of Trade and Industry (note 121) at 34-36.

¹²⁶ Cp. as well American Bar Association Section of Business Law Committee on Corporate Laws 'Report on South African Companies Act No. 61 of 1973 and Related Legislation' available at www.sn.apc.org/usaidsa/usaidsa/corporate.pdf (accessed 28 July 2005) 14.

way¹²⁷ given the fact that it is obviously modeled after the Canada Business Corporations Act 1985 (notabene a fore rider of modern capital rules).

To understand the development of future South African Company Law it is of importance to mention that a team of five American lawyers in their capacity as members of the Committee on Corporate Laws of the Section of Business Law of the American Bar Association were invited by the South African Companies Registration Office ('SACRO') to analyze possible amendments to the Companies Act 1973 in connection with the review of the Companies Act. This fundamental survey resulted in the release of the 'Report on South African Companies Act No. 61 of 1973 and Related Legislation' ('the Report') in December 2001.¹²⁸ It is noteworthy that two of the five lawyers are still closely involved in the current corporate law review process as part of the 'international reference team'. Facing this background it is not surprising that the manner in which corporate finance issues are approached and the way provisions and principles of the Companies Act are put in question in the current reform process reminds one very much of the solutions found in the Revised Model Business Corporation Act. It can therefore be expected that the definitive version of the capital rules in the reformed Companies Act (currently scheduled for February 2007) will presumably not differ much from the American predecessor.

The major recommendation of the report in respect of the capital rules is the deletion of the concept of par value and the related concept of stated capital throughout the Companies Act. According to the Report there is no need for this concept anymore given the fact that the 1999 amendments to the Companies Act have already abandoned any reliance on par value as a standard for the company's power to pay dividends or make other distributions. This recommendation is explained in the following terms: *"Par value was originally developed in the early days of corporations to insure 'equitable contribution,' i.e., equal pro rata payment by stockholders for stock issued by the corporation. This purpose was long ago abandoned as economically unrealistic. Subsequently, par*

¹²⁷ Cp. Department of Trade and Industry (note 121) at 36.

¹²⁸ American Bar Association (note 126).

*value and its corollary, stated capital (par value per share multiplied by the total number of shares outstanding), were employed as part of an equation determining whether the corporation could pay dividends or make other distributions to its stockholders. Under this equation, a corporation may not pay a dividend or make another distribution unless the sum of its assets at least equals the sum of its liabilities and its stated capital. To put it in other words, a corporation could make distributions only out of "surplus." With the development of low-par and no-par stock, this reason for par value has also evaporated. Today, it is widely recognized that par value, especially a low par value, is economically insignificant and artificial. Accordingly, in the mid-1980s, the Model Act abolished par value altogether. In its place, Section 6.40 of our Model Act substituted the equity and balance-sheet solvency tests, which we note that South Africa has also adopted as the standard for acquisition of its shares by a company (Section 85(4)) and for payments to shareholders (Section 90(2))."*¹²⁹

In a consequent abandonment of the par value concept s 81 of the Companies Act (issue of shares of par value at a discount) should as well be deleted as there is no economic connection between par value and the price at which shares are issued by the company.¹³⁰ The representatives of the American Bar Association see no reason why the company should not be able to issue shares at whatever price it can get, even though such a price might be lower than par value - a concept anyway to be abandoned.¹³¹ As regards s 85 of the Companies Act (*Company may under certain circumstances acquire shares issued by it*) the report recommends giving up the requirement of a special resolution as a precondition for share repurchases. This requirement would in any case be satisfied by a boilerplate resolution presented to the shareholders every year which would not provide any significant protection to them.¹³² Furthermore a special resolution

¹²⁹ American Bar Association (note 126) at 14-15; cp. as well Department of Trade and Industry (note 121) at 17, where an almost identical wording is used in order to recommend the review of capital rules. But again, the part that South Africa has already adopted in 1999 an equity and balance-sheet solvency test similar to the Revised Model Business Corporation Act is suppressed in the Guidelines.

¹³⁰ American Bar Association (note 126) at 15.

¹³¹ Consequently, s 82 regarding no par value shares should as well be deleted.

¹³² American Bar Association (note 126) at 15.

should not be required for distributions to shareholders according s 90 of the Companies Act as it has the same economic effect on the company as share repurchases (where such a resolution is as well not required). Therefore the Report suggests to delete s 85 (1) - (3) of the Companies Act.¹³³ As regards preference shareholders the Report would welcome a clarification whether their preference rights should be treated as liabilities when determining the power of the company to acquire its shares.¹³⁴ Additionally, the Report recommends a more explicit statement in ss 85-87 according to which the acquisition of shares on a non-pro rata basis is generally permitted.¹³⁵ As regards s 90 (1) of the Companies Act, the Report recommends the deletion of the requirement that distributions to shareholders must be authorized by the articles of the company since this would again simply lead to a respective boilerplate provision in the articles.¹³⁶ Since after the Companies Amendment Act 1999 there is no need to rely on profits of the company in order to acquire its own shares or to make distributions to its shareholders it seems inconsequent that s 98 of the Companies Act (*Redeemable preference shares*) still resorts to the concept of 'redemption of redeemable preference shares out of profits'. The Report therefore recommends amending s 98 so as to bring it in conformity with s 74 and 90.¹³⁷ And last but not least the Report regards s 38 of the Companies Act (*No financial assistance to purchase shares of company or holding company*) as outdated. Modern corporate practice would require that no limit with regard to the provision of financial assistance for the purchase of the company's shares should be set anymore.¹³⁸

The Guidelines have almost verbatim taken up the recommendations of the Report with regards to the presently interesting capital rules which represent certainly one of the most forward-looking parts of the extensive Company law

¹³³ American Bar Association (note 126) at 15-16.

¹³⁴ American Bar Association (note 126) at 16.

¹³⁵ American Bar Association (note 126) at 16.

¹³⁶ American Bar Association (note 126) at 17.

¹³⁷ American Bar Association (note 126) at 17.

¹³⁸ American Bar Association (note 126) at 11.

review currently underway in South Africa.¹³⁹ The DTI has planned to consult a whole range of stakeholders as well as further local and international experts.¹⁴⁰

With regard to capital rules the debate will deal with the following questions:

- Should the par value and stated capital concept be abolished in the South African Companies Act? What may be the resulting complications of the abolition and how can such complications be dealt with?
- Should the board of directors be given an open power to endorse equity financing for the company without previous shareholder consent?
- Is there still any need to prohibit or restrict the issuance of shares at a discount or should s 81 and s 82 be abolished? Should the company be therefore allowed to issue its shares at whatever price it can get?
- Should s 85 be brought in congruence with s 90 in respect of the requirements and the additional constraint of a special resolution be abolished? Any share repurchase and distribution to shareholders would then be only subject to a solvency and liquidity test.
- Should preference shareholders receive explicit protection within the solvency test of s 85 and s 90 by treating their preference rights as liabilities of the company?
- S 98 (*redemption of redeemable preference shares*) should be brought in line with the share buy-back (ss 85-88) and dividend provisions (s 90).
- Should a company not be prohibited or limited anymore in giving financial assistance to purchasers of its shares? Should the prohibition in s 38 be deleted or rather added with more exceptions? If it is deleted, what kind of safeguards would protect against misuse by directors or majority shareholders?

¹³⁹ Department of Trade and Industry (note 121) at 17, 34-35.

¹⁴⁰ Department of Trade and Industry (note 121) at 52-53.

2. Legal situation in Switzerland

2.1. Capital maintenance rule

2.1.1. Introduction

As opposed to South African Company Law and in congruence with European Company Law share capital protection is still a fundamental part of Swiss Company Law¹⁴¹. The respective rules can broadly be divided into such concerning the provision of share capital, such concerning the maintenance of share capital and such giving a coercive signal to embark on emergency measures in case of substantial capital loss.¹⁴² The reason why share capital deserves special protection has been explained with the limited liability of the company.¹⁴³

When considering the capital protection rules in Switzerland it is certainly necessary to start with the notional size 'par value share capital'. The principle is stated in Article 620 s 1 of the Swiss Code of Obligations (OR): "*A corporation is a company with its own company name whose predetermined capital (share capital) is divided into parts (shares) and whose liability is limited to the Company's assets.*" The minimum share capital according to Article 621 OR is one hundred thousand Swiss Francs whereby upon incorporation of the company, a contribution of at least twenty percent of the par value of each share must be made. The contribution must however in all cases total at least fifty thousand Francs (Article 632 OR). The par value share capital is a fixed amount expressed in the currency of Switzerland (CHF) which is stated in the articles of incorporation of the Company as well as in the Commercial Register at the place of the domicile of the Company. It is divided into a certain amount of shares each having a par value expressed in the local currency which shall not be less than 1

¹⁴¹ The notion 'Swiss Company Law' not only refers to the law of share holding companies (corporations) but as well to some other company forms. However, for the purpose of this assignment 'Swiss Company Law' shall be understood in the restricted sense of 'Swiss Corporation Law' in order to use a consistent terminology.

¹⁴² P Böckli *Schweizer Aktienrecht* 3ed (Zürich Basel Genf: Schulthess Juristische Medien AG 2004) s 97.

¹⁴³ R von Büren/WA Stoffel/K Schnyder/C Christen-Westenberg *Aktienrecht* (Zürich: Schulthess, 2000) s 197.

cent (Article 622 s 4 OR). Shares can only be issued at or above par value (Article 624 OR). The multiplication of the share par value with the amount of shares is equivalent with the par value share capital.

The function which has been attributed to the concept of par value capital is fourfold: first it represents a minimum capital which has to be paid in by the shareholder (*capital provision*), secondly, as a principle of transparency, the founding members of the company are obligated to publicize the minimum capital, thirdly it represents a limitation for distributions to shareholders as the minimum capital cannot be paid back to them (*capital maintenance*) and fourthly it is a bar for distributions if - after deduction of all liabilities - the minimum capital is not covered anymore by genuinely valued assets. After such a capital loss has occurred this prohibition lasts as long as the minimum capital has not been recovered out of future profits (*capital maintenance*).¹⁴⁴ The par value share capital system is usually justified with providing creditor protection. But especially this alleged function has been put in question in doctrine and the par value share system has been subject of criticism which will be looked at closer below section 2.2.

The systematic how the capital maintenance rule in Switzerland will be discussed in the following will slightly deviate from the one used in the South African part. The reason for this is that the capital maintenance doctrine in Switzerland is not afforded the same independent and outstanding significance as it has or at least had in common law countries. The capital maintenance rule is rather part of a holistic concept of share capital protection as described above and is hardly independently put in question in doctrine. The critical analysis starts at a logical step right ahead that is with the notional size of share capital as stated in the capital account.¹⁴⁵ The legal size 'share capital' is a bar figure ('Sperrziffer') in the balance sheet. The completion of different functions is related to this figure, only one of them is the maintenance of capital. In order to understand the legal situation in Switzerland with respect to the capital maintenance rule it is therefore

¹⁴⁴ Böckli (note 142) at s 9.

¹⁴⁵ In the following the notion 'share capital' will be used in this sense without explicitly referring to the share capital 'as stated in the share capital account'.

necessary to summarize in the following all of the three functions allegedly justifying the continual application of the share capital concept.

2.1.2. The Raise of Share Capital (Principle of Coverage)

The principle of coverage ('Deckungsprinzip') guarantees that the share capital as stated in the Articles of the company as well as in the Commercial Register is actually raised and can be freely (without conditions and in respect of the whole amount) used by the company. The subscription of the share capital - whether during the founding process or during the increase of the share capital - requires the unconditional commitment of the present or prospective shareholder to make a contribution equal to the issue price (Article 630 cypher 2 OR). The founders must establish in the deed of incorporation that the promised contributions correspond to the total amount of the issue (Article 629 s 2 cypher 2 OR). As seen above shares may only be issued at or above par value (Article 624 s 1 OR) and the share capital must be paid up to a minimal amount (20% of the par value of each share, but in all cases at least CHF 50'000; Article 632 OR). Until the legally required minimal amount is not paid in, the company cannot come into legal existence since it cannot obtain the necessary entry into the Commercial Register or, as far as an increase of share capital is concerned, the increase will not become valid until the entry into the Commercial Register is conferred upon the company.¹⁴⁶ There are many more provisions which are directed at the realization of the principle of coverage for example, Article 632 OR where money contributions must be deposited at the exclusive disposal of the Company at an institution subject to the Federal Law of November 8, 1934, Relating to Banks and Saving Banks. The institution can only release the amount upon the Company's entry in the Commercial Register. Of foremost importance in realization of this principle is Article 634 OR concerning contributions in kind where protection against fraud is foremost required: *"Contributions in kind are deemed to cover only if they are made based upon a written or publicly notarized contract of contributions in kind, if the Company, upon its entry in the Commercial*

¹⁴⁶ von Büren/Stoffel/Schnyder/Christen-Westenberg (note 143) at s 210.

Register, may, in its capacity as owner, immediately dispose thereof, or receive an unconditional claim for entry in the Real Estate Register and if a founders' report together with the confirmation of examination is presented." All these requirements make sure that at least in the moment when the company comes into existence or when the increase of capital has taken place the commercially active public may trust in the existence of the capital as publicized in the Articles of the Company and in the Commercial Register.

2.1.3. Maintenance of Capital

(a) Distributions to shareholders

As explained above, the share capital is a rigid, notional figure which does not depend on the development of the business of a company. It is reflected on the right hand side of the balance sheet and indicates the amount which should at least be covered by the assets of the company at every point in time. Up to the amount of the share capital a company may use its assets only for paying its debts. Shareholders have no right to claim return on their contribution (Article 680 s 2 OR). A repayment of the share capital to the share holders is possible only upon liquidation of the company or partial liquidation, i.e. capital reduction.¹⁴⁷ In Switzerland share capital is not considered as a debt of the company towards its shareholders.¹⁴⁸

Not only is a direct repayment of the share capital prohibited - distributions out of profits are only allowed if the balance sheet of the company actually attests that a profit has been generated.¹⁴⁹ In order to make sure that profits are properly established Swiss Law Accounting Rules apply for the rendering of accounts.¹⁵⁰ It follows the principles of completeness of annual financial statement, of clarity and essentiality of statements, of prudence and of consistency in presentation

¹⁴⁷ T Guhl/A Kummer/JN Druey *Das Schweizerische Obligationenrecht* 8ed (Zürich: Schulthess Polygraphischer Verlag AG, 1995) 631.

¹⁴⁸ von Büren/Stoffel/Schnyder/Christen-Westenberg (note 143) at s 215; unlike in South Africa where it is held that a company's capital accounts represent a 'notional liability' of the company, cp. Blackman/Jooste/Everingham (note 16) at 5_16.

¹⁴⁹ von Büren/Stoffel/Schnyder/Christen-Westenberg (note 143) at s 213; Guhl/Kummer/Druey (note 147) at 631.

¹⁵⁰ C Baudenbacher in H Honsell/P Vogt Nedim/R Watter (eds) *Basler Kommentar zum Schweizerischen Privatrecht, Obligationenrecht II, Art. 530–1186 OR* 2ed (Basel Genf München: Helbing & Lichtenhahn, 2002) s 16 Art. 620.

and valuation. The setting off of assets and liabilities, as well as of expenses and income is prohibited (cp. Articles 662 ff. OR).

In order to prevent the distribution of an increase in value not actually realized and therefore to prevent the drain of liquidity the Swiss Law Accounting Rules allow with few exceptions only the realized profit to be assigned to the balance sheet profit (as the decisive size for the declaration of dividends according to Article 675 s 2 OR).¹⁵¹ Capital assets are for example to be valued at a maximum of the acquisition or manufacturing costs less the necessary depreciation (Article 665 OR). The same applies for raw materials, semi-finished, finished products and merchandise (Article 666 s 1 OR). If the acquisition or manufacturing cost are higher than the market value generally applicable on the date of the balance sheet, then such market value is determinative (Article 666 s 2 OR). In every case, assets can never be valued higher than their value to the business on the date of the balance sheet (Article 960 s 2 OR).¹⁵²

Distributions to shareholders without a corresponding profit determined according to Swiss Law Accounting Rules would amount to a repayment of share capital. Dividends can only be paid out of a duly established balance sheet profit or out of reserves created for this purpose (Article 675 s 2 OR). Similarly, share repurchases are prohibited as long as there is no freely disposable equity available (Art. 659 s 1 OR). As long as the assets as well as the liabilities are not covered by fairly valued assets all profits generated by the company must first and exclusively be used to recover the capital deficiency. Until full coverage is achieved the prohibition of distribution persists.¹⁵³

(b) Legal reserves and reserves according to the articles of incorporation

The ‘Sperrziffer’ share capital may be increased by legal reserves (cp. Articles 671 OR ff.). 5% of the annual profit must be allocated to the general reserve until it has reached 20% of the share capital (Article 671 s 1 OR). Even after having

¹⁵¹ Böckli (note 142) at s 105.

¹⁵² P Forstmoser/A Meier-Hayoz/P Nobel *Schweizerisches Aktienrecht* (Bern: Verlag Stämpfli+Cie AG, 1996) § 50 s 230 ff.

¹⁵³ Böckli (note 142) at s 151.

reached the statutory amount allocations must continue in certain instances: for example 10% of the amounts which are distributed as a share of profits after payment of a dividend of 5% or any surplus over par value upon the issue of new shares after deduction of the issue cost must be credited to the general reserves (Article 671 s 2 cypher 1 and 3 OR). And in case of a share repurchase an amount corresponding to the acquisition value must be allocated to legal reserves designated as reserves for own shares (Article 659a s 2 OR). Reserves for own shares may in case of alienation or cancellation of shares be dissolved to a maximum of their acquisition value (Article 671a OR). General legal reserves which are not exceeding half of the share capital may however only be applied to cover losses or for measures bound to maintain the company in bad business times, to counteract unemployment, or to soften its consequences (Article 671 s 3 OR).

The articles of incorporation may according to Article 672 s 1 OR provide even for higher amounts than 5% of the annual profit to be allocated to the reserve or/and that the reserve must amount to more than 20% of the share capital prescribed in Article 671 s 1 OR. Only after the allocations to the legal reserve and to the reserves provided for by the articles of incorporation have been made, dividends may be declared. The bar figure is therefore strictly speaking not limited to the share capital. It can be increased by legal and statutory reserves (not destined for the purpose of profit distribution).

(c) *Acquisition of own shares*

As already mentioned above the acquisition of a company of its own shares can as well constitute a form of redistribution of share capital. Liquidity is taken away from the company which could have otherwise been invested according to the purpose of the company. Real assets are replaced through participation on preexisting net assets and become thereby a non value asset.¹⁵⁴ This participation of the company in its own assets appears henceforth in the form of treasury shares on the left hand side of the balance sheet whereas the share capital on the right hand side remains intact. Unlike the precaution measures

¹⁵⁴ Böckli (note 142) at s 196; Forstmoser/Meier-Hayoz/Nobel (note 152) at § 50 s 131 ff.

provided in the liquidation or capital reduction procedure distributions of the company's liquidity through a share repurchase would take place without safeguards for creditors or minority shareholders.¹⁵⁵ Share capital protection would be rendered illusory. In consideration of these potential risks, share repurchases were first forbidden in Swiss Company Law, then between 1936 and 1992 prohibited with few exceptions and since 1992 allowed within strict limits: the total par value of treasury shares may not exceed 10% of the share capital (Article 659 s 1 OR) and as already mentioned above the acquisition must be effected through freely disposable equity over the necessary amount. The same limitations apply for share repurchases executed by a subsidiary of the company in which the company holds majority participation (Article 659b s 1 OR). The voting right connected with treasury shares cannot be executed, i.e. remains inactive (Article 659a s 1 OR).

(d) Financial assistance to purchase shares

A provision similar to s 38 (*No financial assistance to purchase shares of company or holding company*) of the Companies Act does not exist in Swiss Company Law. Different provisions make it however clear that at least the issue of shares might not be validly taken place if the company itself provides the financial means necessary for the acquisition. The subscription on incorporation requires according to Article 630 s 2 OR an unconditional commitment to make a contribution equal to the issue price. Before the necessary contribution is not fully paid in on a special account the company will not be registered in the Commercial Register and therefore not come into legal existence. On incorporation the contribution may only be made in money or in kind (Articles 633 ff. OR). Subsequent performance of (initial) contributions can as well be made by set-off (Article 634a s 2 OR). As far as an increase of share capital is concerned Article 652c OR provides that contributions must be performed in accordance with the provisions on incorporation if the law does not provide otherwise. Contributions may therefore only be made in money, in kind or by set-off.

¹⁵⁵ Böckli (note 142) at s 198.

Consequently an issue of shares cannot be financed by the company itself, the necessary contribution must come from the acquirer.

However, there is no provision which would allow such a conclusion in relation to a share purchase. It is on the contrary acknowledged that a company may for example confer loans to its (actual or future) shareholders even though such a transaction might be critical.¹⁵⁶ The loan is in this case normally not invested according to the purpose of the company. Such an operation can render the members of the board of directors liable according to Article 754 s 1 OR if it is connected with a violation of the duty of care. This would be the case for example if the board of directors does not - when conceding the loan - allocate the risk rationally or does not apply at arms length conditions or if the rules of share capital protection are thereby violated, in the extreme case if the granting of a loan would amount to a reimbursement of the shareholders contribution.¹⁵⁷

As a result it must be concluded that even though a company (or its subsidiary) is in principle not prohibited from granting financial assistance to third persons for the purchase of its shares (or for the purchase of the shares of the holding company) the board of directors is running thereby a considerable risk in becoming liable for damage suffered by the company, shareholders and creditors.

(e) *Share capital reduction*

The only way in which the share capital of a company going concern can legally be diminished is through a formal reduction procedure according to Articles 732 ff. OR. A reduction below the required minimum capital of CHF 100'000 is however prohibited (Article 732 s 5 OR). There are three different kinds a capital reduction may take place: first, a simplified procedure in the event of a capital deficiency in order to readjust the balance sheet, secondly, a simplified procedure in case the reduced share capital is simultaneously replaced by new fully paid in capital to the preexisting level and thirdly the presently interesting case where the reduction takes place in order to return the respective amount to

¹⁵⁶ Böckli (note 142) at s 544.

¹⁵⁷ Böckli (note 142) at s 545.

the shareholders. In this last case the share capital reduction is material, i.e. it equals a partial liquidation of the company, wherefore the need for safeguard measures is perceived as evident. It entails changes on both side of the balance sheet: on the right hand side the bar figure share capital is reduced whereby the left hand side is diminished due to the disposition over the newly available assets.¹⁵⁸

The legal procedure applying to a material capital reduction can be summarized as follows: First, it must be established by a special auditors' report that claims of the creditors are fully covered in spite of the intended share capital reduction. This is a precondition that a general meeting of shareholders can be held and a resolution over the capital reduction can be passed with the necessary amendment of the respective article of incorporation (Article 732 s 1 OR). The author of the auditors' report must be present at the general meeting of shareholders (Article 732 s 2 OR). The resolution must state the findings of the auditors' report and indicate the ways and means by which the reduction of the share capital shall be implemented (Article 732 s 3 OR). After a positive resolution within the shareholder meeting the board of directors must publish the decision three times in the Swiss Official Gazette of Commerce. Furthermore, it must notify the creditors that they may request satisfaction or security within two months calculated from the third publication in the Swiss Official Gazette of Commerce (Article 733 OR). After the expiration of the time period set for the creditors and after all creditors who have filed claims have been satisfied or secured the reduction of share capital may be implemented. The necessary entry into the Commercial Register however is only conceded if it is established by a notarized deed that the provisions in Articles 732 ff. OR have been complied with (Article 734 OR).

2.1.4. Signal for emergency measures

The third part of capital protection rules is concerned with the situation when a company suffers a substantial capital loss. In broad terms, the rules tell the board

¹⁵⁸ Böckli (note 142) at s 336; Forstmoser/Meier-Hayoz/Nobel (note 152) at § 53 s 14-17.

of directors in case of continually decreasing equity when and how to embark on emergency measures. Depending on the degree share capital and legal reserves are not covered any more by duly valued assets, Swiss Company Law institutes a so called 'warning bell'¹⁵⁹. A continued trading without equity base shall be prevented in the interest of shareholders, creditors (especially potential new ones) and employees.¹⁶⁰ The 'warning bell' rings if the last annual balance sheet shows that half of the share capital and the legal reserves are no longer covered. In this case the board of directors must without delay call a general meeting of shareholders and propose a financial reorganization (Article 725 s 1 OR). In case of a substantiated concern of over-indebtedness, an interim balance sheet must be prepared and submitted to the auditors for examination. If the interim balance sheet shows that the claims of the Company's creditors are not covered anymore¹⁶¹ then the board of directors must notify the judge unless creditors can be found who subordinate their claims to the extent of insufficient coverage (Article 725 s 2 OR). Upon being notified, the judge either adjudicates the bankruptcy or postpones it if so requested by the board of directors or a creditor provided that there is a prospect of a financial reorganization (Art. 725a s 1 OR).

2.2. Criticism on the share capital concept

As discussed in the introduction, Swiss Company Law is still based on the par value share capital system. Continental European Company Law in general differentiates between 'notional no par value shares' (foremost 'Stückaktien') and 'real no par value shares' (so called 'echte nennwertlose Aktien'). According to this differentiation South African Company Law currently knows only the 'notional no par value shares' but is otherwise - as shown above - still based on the par value or stated capital concept. The introduction of 'real' as opposed to 'notional no par value share' would imply the complete abolishment of the no par value share capital concept. Both of these share categories are still unknown in Swiss Company Law whereas European Company law allows at least the 'notional no

¹⁵⁹ Böckli (note 142) at s 101b, 106; Guhl/Kummer/Druey (note 147) at 634-635; Forstmoser/Meier-Hayoz/Nobel (note 152) at § 50 s 193 ff..

¹⁶⁰ Böckli (note 142) at s 713.

¹⁶¹ Neither to ongoing business values or liquidation values.

par value share'. Both, German and French Company Law have introduced this share category in 1998 in order to facilitate the introduction of the EURO.¹⁶²

As far as 'notional no par value shares' (in the form of 'Stückaktien') are concerned it is quite undisputed in doctrine that they should be introduced in Swiss Company Law as well. The reason being is that the 'par value' concept is misleading in the sense that it led to the wrong assumption that this figure attributed to each share, would have something to do with its real value which is clearly not the case. The par value of each share is nothing more than a mathematical operation, i.e. the division of the share capital through the number of issued shares. The share capital again is independent of the value of the assets within the company or the economic development of a company; it is only a legal size without economic significance.¹⁶³ With the proceeding business activities of a company share capital loses every relation to the effective value of the company.¹⁶⁴ The economic value of each share can therefore not be deduced from the share capital (or at least not longer than during a few logical seconds on incorporation of the company) but must be understood as a fractional participation on the assets of a company. With the introduction of the 'notional no par value shares' there would be henceforth no indication of the par value on the share certificate, in the Articles of Incorporation or in the Commercial Register anymore. However, every share would still have a notional or arithmetic par value - even though invisible - which is arrived at by dividing the share capital by the number of issued shares.¹⁶⁵ The reform would be of a rather formal nature with the one didactical advantage that the wrong assumption a share's value would depend on the share capital would become less likely. The number of shares having no par value could be increased or diminished without necessarily at the same time increasing or decreasing the share capital. The par value would

¹⁶² cp. *Stückaktiengesetz* of 25 March 1998 and revision of Article 268 LSC of 2 July 1998; HC von der Crone 'Bericht zu einer Teilrevision des Aktienrechts: nennwertlose Aktien' (2002) 1 *Reprax* 1 at 7.

¹⁶³ WA Stoffel 'Abschaffung des Nennkapitalsystems im schweizerischen Aktienrecht?' (2001) 23 *SJZ* 533 at 536.

¹⁶⁴ von der Crone (note 162) at 5.

¹⁶⁵ P Böckli 'Nennwertlose Aktien und Kapitalschutz' in RJ Schweizer/H Burkert /U Gasser (eds) *Festschrift für Jean Nicolas Druey* (Zürich/Basel/Genf: Schulthess, 2002) 331 at 337.

in this case be changed implicitly without an adjustment on every share certificate. Any change of par value would therefore remain without consequence, formally as well as materially.¹⁶⁶

As already discussed, the par value of a share says nothing about the economic value of a share. It can therefore be questioned whether the par value should still be retained even though only in the form of 'notional no par value shares'. Why not entirely abandon the par value or share capital concept and introduce the 'real par value share'? Without a share capital the present underpinning of the threefold capital protection function would disappear.¹⁶⁷ The question is therefore whether this function still justifies the preservation of the share capital. Does share capital protection, particularly the capital maintenance rule, work satisfactorily in praxis and deliver on what it was introduced for?

The capital maintenance rule is usually justified with the fact that a fundamental conflict of interests is part of every corporation with limited liability.¹⁶⁸ The conflict of interests exists between shareholders, foremost majority shareholders, which - driven by short term gain maximizing objectives - are disposed to draw as much equity from the company to their own funds as possible and other stakeholders, especially creditors who have trusted in the existence of the publicized share capital before agreeing to trade with the company.¹⁶⁹ Such equity drain may be realized for example in the form of dividends, hidden profit distribution or loans to shareholders. The principle aim of share capital protection is therefore to prevent especially majority shareholders and members of the management from an unlimited and uncontrolled withdrawal of company's funds.

However, it has been held that the relation between share capital and equity has changed over the last century in a way rendering the usefulness of share capital protection questionable. During the last century it was common that a generated profit would normally almost entirely be redistributed to the shareholders in the form of dividends. After the distribution of the dividends the equity was typically

¹⁶⁶ Böckli (note 165) at 340.

¹⁶⁷ Böckli (note 165) at 343.

¹⁶⁸ A company as understood in this assignment is always a corporation with limited liability.

¹⁶⁹ Böckli (note 142) at s 109, 111.

again identical with the share capital. In consequence the law protected automatically almost the whole equity as presented on the balance sheet of a given company from being redistributed to the shareholders. For the last approximate 100 years the dividend policy however has changed, both in listed and unlisted companies, whereas the respective law remained almost untouched. Dividend policy is today rather aimed at a sustainable retention of profits than at its distribution. Reserves (besides the legally prescribed one) have deliberately been built up within the companies and the normal pay-out ratio has dropped to between 25% and 40%. Only in very few sectors for example, with banks, 50% of the profits are still distributed. As a result the reserves in an average successful, 20 year old company (and most of the small and medium-sized companies in Switzerland have around this age) have grown exponentially and the share capital has typically shrunk to a small, insignificant portion of the equity. The consequences are evident: the bar function of the share capital protects only a small, insignificant portion of the entire equity and becomes thereby significantly less important. The bigger part of the equity is excluded from the capital protection rules and is available for dividends to shareholders.¹⁷⁰ The debts of such companies are normally far higher than their share capital and a rational potential creditor would never deduce from the company's share capital to its creditworthiness.¹⁷¹ A contractual creditor can ask for additional, sufficient safeguards but the protection of non-contractual creditors through the share capital system has become largely illusory. The introduction of a personal liability of the founders and shareholders in case of an obvious undercapitalization would be of far more value to non-contractual creditors.¹⁷² But even as far as this remaining portion of the equity, the share capital, is concerned the capital maintenance rule can be evaded and the whole protection function of the share capital be annulled through returning funds by way of loans granted by the company to its shareholders.¹⁷³

¹⁷⁰ Böckli (note 142) at s 112 ff.

¹⁷¹ Stoffel (note 163) at 536.

¹⁷² Stoffel (note 163) at 536.

¹⁷³ Böckli (note 165) at 344.

Finally, as far as the 'warning bell' function of the share capital is concerned it often 'rings' too late since it refers to a historic size, i.e. the share capital. The board of directors is therefore often obliged to embark on emergency measures not until most of the equity is already lost. In such a situation it is usually too late to realize a turn around of the negative business development.¹⁷⁴ Economically really important alarm signs can therefore not be derived from the share capital.¹⁷⁵

Besides these specific points of criticism there are also voices in Swiss legal doctrine which criticizes the share capital system as a whole and would like to see it either abandoned in favor of a system modeled along the lines of the American Revised Model Business Corporation Act (American Model) or at least substantially modified in order to achieve a more flexible structure of the share capital. The advantages of the American Model are perceived in its pragmatism and result orientation. The continental European share capital system - despite its stringency and comprehensiveness it might have developed over the last century - is in contrast characterized as formal and rigid with a tendency to bypass the real problems.¹⁷⁶ The argument is not that the non share capital system would provide better but equivalent creditor protection wherefore the justification for the share capital concept becomes questionable. Even though the important law authorities on this field agree that the share capital system as actually provided for in the Swiss Code of Obligations is inexpedient and too rigid to meet the actual economic and social challenges of Company Law and would welcome a more flexible share capital structure the recommended alternative models differ quite considerably. In the following chapter, three schemes for a more flexible share capital structure will be discussed in more detail.

¹⁷⁴ Böckli (note 165) at 345.

¹⁷⁵ Stoffel (note 163) at 536.

¹⁷⁶ Stoffel (note 163) at 539, 542; von der Crone (note 162) at 4.

2.3. Schemes for a more flexible share capital structure

(a) The most advanced proposal demands a complete abolishment of the share capital system following the American Model.¹⁷⁷ Creditors are thereby not protected by share capital protection rules but through private instruments like ratings and contractually agreed ratios to be observed by the company or - especially as far as non-contractual creditors are concerned - by the personal liability of founders and shareholders in case of significant undercapitalization. According to this scheme creditors are not per se better off when the share capital system is abolished but, not worse either since share capital protection would provide only an illusory security. According to the share capital protection rules the board of director is indeed not allowed to return assets up to the amount of the share capital to its shareholders. But within the limits given by its duty of care it is not prevented from embarking on very risky undertakings whereby the whole equity can be ventured to the disadvantage of creditors and minority shareholders.¹⁷⁸

Share capital is fixed on incorporation. It can later be changed (increased or reduced) in principle only by a resolution of the shareholder meeting and under the observance of several safeguards especially as far as share capital reductions are concerned. The supremacy to decide over the share capital of a company is therefore on incorporation as well as during its existence with the general meeting of shareholders.

In the non share capital system according to the American Model the board of directors is in contrast vested with large authority. Representative for this fact is already the issue of shares: Shares are issued in the amount and in the form considered necessary for the intended business activity by the board of directors.¹⁷⁹ The eligible consideration is very broad and ranges from contributions in money, kind or (rendered and future) services. Opposed to this broad discretion stands the general liability of founders and shareholders vis-à-

¹⁷⁷ Stoffel (note 163) at 539, 542; WA Stoffel 'Nennwertlose Aktien für die Schweiz? Plädoyer für eine Reform des Aktienrechts' *NZZ* 19/20 May 2001 at 29.

¹⁷⁸ Stoffel (note 163) at 538.

¹⁷⁹ Stoffel (note 163) at 539.

vis creditors in case of undercapitalization and the liability of the board of directors in case it treats shareholders non-equal.

In Swiss Company law the issue of shares (cp. Articles 632 ff. OR) is a very formalistic and highly sensitive process as seen below 2.1.2. whereas on the other hand a general liability for undercapitalization does not exist. As far as share capital increases are concerned the system in Switzerland has already become more flexible since the last revision in 1991 with the introduction of the authorized increase of capital (cp. Article 651 OR)¹⁸⁰ but is still lacking behind the American Model. The power for share capital increases ultimately remains with the shareholder meeting whereas in the American Model the issue of shares is in the power of the board of directors and is only limited by its fiduciary duties, especially the duty of care vis-à-vis the existing shareholders, in order to prevent so called oppressive issuances.¹⁸¹

Liability of corporate bodies in the non capital system never depends on a technical notion like share capital. It is rather based on general principles like the before mentioned fiduciary duties, the duty to safeguard the interests of the company as well as the duty to inform shareholders accurately. The broad formulation of these duties serves creditor as well as shareholder interests and has a wide potential for further law development in this area. In Switzerland the liability of corporate bodies in contrast is most often deduced from the notion share capital and its coverage on a specific point in time (Article 725 OR). This formalistic approach hardly possesses potential for a result orientated further development.¹⁸²

According to the proponents of this approach the non share capital system has the advantage to address the real problems. The general liability principles allow the finding of appropriate results since they are open for interpretation and

¹⁸⁰ According to Article 651 s 1 OR the general meeting of shareholders can now, by amendment to the articles of incorporation, authorize the board of directors to increase the share capital within a period of no longer than two years. According to s 2 the par value by which the board of directors may increase the share capital must be indicated in the articles of incorporation and cannot exceed half of the current share capital. Within the scope of authorization the board of directors can implement the increases of the share capital (s 3).

¹⁸¹ Stoffel (note 163) at 539.

¹⁸² Stoffel (note 163) at 541.

development. The non share capital system is rather directed at the material result than at the protection of formalistic procedures. Further law developments in response of changing requirements do not necessarily demand a law reform. The rigid share capital system on the other hand might be simpler in application but is often bypassing the real problems whereas relatively unproblematic procedures are rendered unnecessarily complicated. It clings to formalistic and systematic structures which afford a rather deceiving security. A non share capital system would allow a commitment to material and economic principles, e.g. the introduction of general liability rules for the board of directors, thereby replacing the formalistic control derived from the share capital.¹⁸³

(b) A less resolute proposal welcomes in fact the introduction of 'real par value shares' but without giving up capital protection rules.¹⁸⁴ It acknowledges the advantages of giving up par value shares (flexibility and simplicity).¹⁸⁵ The capital protection is however still perceived as a necessary consequence that a company may participate in commerce with limited liability. Furthermore, it is regarded as indispensable to protect creditors as well as minority shareholders against majority shareholders who are inclined to drain capital away from the company after incorporation.¹⁸⁶ In other words, the American Model which does not acknowledge the idea of creditor protection via capital protection rules is not adopted in this model. On the contrary, the question is asked whether there is a way to modernize and strengthen capital protection rules in Swiss Company Law. As already explained above, by introducing the 'real non par value share' the share capital would necessarily fall away as the methodically simple link for capital protection rules.¹⁸⁷ Based on the perceived weaknesses of the share capital system mentioned below section 2.2., the problem to be solved is how

¹⁸³ Stoffel (note 163) at 542-43.

¹⁸⁴ Böckli (note 165); P Böckli 'Revisionsfelder im Aktienrecht und Corporate Governance' (2002) 138 ZBJV 709.

¹⁸⁵ Böckli (note 165) at 342.

¹⁸⁶ Böckli (note 165) at 342.

¹⁸⁷ Böckli (note 165) at 343.

capital protection can be realised without relying on the present reference size share capital.

Whatever size is chosen in order to link the capital protection rules the threefold function which must be fulfilled remain the same in this scheme: the principle of coverage, the capital maintenance rule and the signal for emergency measures. The rules which apply in order to secure the raising of capital and prevent fraud on issuance apply unchanged as far as the coverage of the issue prize by immediately disposable net assets is concerned. The issue prize upon incorporation has henceforth to be fully paid in over the subscribed amount (and not only over a reduced amount as presently provided for in Article 632 OR). The differentiation between par value and premium does not exist anymore as a consequence of the abolishment of the share capital system. The board of directors decides over the issue prize with due care which will normally lead it to the actual market value.¹⁸⁸

As far as the capital maintenance rule is concerned the reference size 'share capital' shall henceforth be replaced by 'capital reserves' as stated in the last audited annual balance sheet. The reference size is automatically increased every time capital is brought in effectively. The increase is limited by the authorized capital. A diminution of 'capital reserves' however is only possible by means of a formal capital reduction according to Articles 732 ff. OR. An offsetting with realised losses is excluded. The fraction of the annual profit which has presently to be allocated to the legal reserves is henceforth allocated to the 'capital reserves' in order to enforce the equity of a company. The possibilities for profit distribution are therefore diminished.¹⁸⁹ Is the 'capital reserve' together with liabilities not covered by fairly valued assets all profits generated by the company must first and exclusively be used to recover this capital deficiency before dividends can be distributed.¹⁹⁰

And finally as far as the 'warning bell' function of the share capital is concerned emergency measures would have to be initiated by the board of directors not

¹⁸⁸ Böckli (note 165) at 347.

¹⁸⁹ Böckli (note 165) at 347-48.

¹⁹⁰ Böckli (note 165) at 348.

only upon half of the share capital and the legal reserves are no longer covered but, upon loss of a third of the total 'capital reserve'. In bringing forward the critical moment to embark on emergency measures to a point in time when the need of restructuring measures becomes apparent due to a continuing loss of equity, it is hoped to improve the prospects of the ensuing turn around measures.¹⁹¹

The requirement of a minimum capital can be retained in this system but now in the form of a minimum 'capital reserve'.¹⁹² Within this scheme 'real no par value shares' are realized and the share capital is - at least formally - abandoned. Capital protection rules are however not only retained but even strengthened. The rigid 'share capital' is replaced by the flexible 'capital reserve'. Through the extension of the amount which is not available for distribution to shareholders it is aimed to make capital protection rules operative again.

(c) According to a third model it is possible to achieve a sufficiently flexible capital structure without introducing 'real no par value share'. This happens foremost by enhancing the authority of the board of directors.¹⁹³ The flexibility of the American Model would not principally lay in the abolishment of the share capital but in the authority conferred upon the board of directors to issue shares up to the amount of the authorized capital. Without this authorization, the capital structure would be rigid with or without the existence of 'real no par value shares'.¹⁹⁴ This model is not so much concerned with capital protection rules even though the decreasing significance of the share capital as a reference size with progressing business activity is acknowledged. But this limited economic significance of the share capital with increasing maturity of a company serves rather as an argument to render it more flexible. Creditor protection should better be enforced by allowing companies to integrate voluntarily additional

¹⁹¹ Böckli (note 165) at 348.

¹⁹² Böckli (note 165) at 350.

¹⁹³ von der Crone (note 162) at 11.

¹⁹⁴ von der Crone (note 162) at 11.

mechanisms like ratings or financial ratios (for example a minimum equity ratio) in their articles of incorporation.¹⁹⁵

It is held that the share capital system as provided for in Swiss Company Law does in its rigidity not meet the requirements of modern corporate finance. The reason being is that the question on what to invest should usually precede the question of how to finance the respective investment. The general meeting of shareholders should therefore be free to confer upon the board of directors a wide authority over financing decisions parallel to its already existing authority over investment decisions. Swiss Company Law however leaves a big say to the general meeting of shareholders as far as financing by equity is concerned wherefore the financing decision is conceptually made before the decision over the investment.¹⁹⁶ Even though share capital has already become more flexible during the last reform process in 1991 with the introduction of the authorized increase of share capital (Article 651 OR) the aim of a flexible share capital structure has only partly been realised. The procedural formalities are still extensive. The authority which can be given by the general shareholder meeting to the board of directors to increase the share capital is only valid for two years. Above all, an analogue procedure for an 'authorized' capital reduction is still not provided; the board of directors lacks every competence within the capital reduction procedure.¹⁹⁷

The proposed model in order to overcome the inflexibility of the share capital in Swiss Company Law is the introduction of a 'capital band' ('Kapitalband'):¹⁹⁸ a company may in its articles of incorporation provide for a 'capital band' in lieu of a fixed share capital. The capital band is defined by a basis and a maximum capital. The basis capital must be raised according to the present provisions on incorporation and capital increases. It can only be reduced by obeying the formal capital reduction procedure (Articles 732 ff. OR). The basis capital henceforth affords the formal security to creditors so far provided by the share capital. But

¹⁹⁵ von der Crone (note 162) at 5.

¹⁹⁶ von der Crone (note 162) at 6.

¹⁹⁷ von der Crone (note 162) at 4.

¹⁹⁸ von der Crone (note 162) at 16-20.

within the capital band it is possible to increase and reduce the share capital by following thereby a simplified procedure. The general meeting of shareholders can introduce a capital band at every point in time with special resolution according to Article 704 OR¹⁹⁹ for a maximum of five years. If not renewed after this period the share capital as it exists at that moment will become fix.

Basis capital and maximum capital have to be stated in the articles of incorporation. The basis capital must be at least CHF 100'000 and the maximum capital may not exceed the basis capital for more than 100%. The introduction of 'notional no par value shares' is welcomed. The increase or the reduction of the basis capital will follow the present provisions concerning the ordinary increase and reduction of share capital. But within the 'capital band' the increase and reduction of the share capital is not only depleted of formalities but henceforth in the authority of the board of directors. As far as capital reductions are concerned the board of directors must indeed make sure that reduced share capital as well as the legal reserves is still covered after the capital reduction. But the notification to the creditors or their right to ask for the provision of security according to Article 733 OR is not applicable anymore.

This model should on the one hand enable the board of directors to react faster and easier to the requirements of adverse conditions and volatile markets and provide on the other hand for a balance of interest between the company in a flexible share capital structure and the creditors in the protection of the share capital.²⁰⁰

2.4. Valuation of the discussed schemes

The three, above discussed, major approaches within the current reform discussion in Swiss doctrine bear on the first sight not many resemblances. An agreement exists as far as the abolishment of par value shares is concerned. But whether this implicates as well the abandonment of the share capital concept or entails only the introduction of the 'notional no par value' shares is not uniformly

¹⁹⁹ Article 704 OR implies a two third majority of the votes represented and the absolute majority of the par value of shares represented.

²⁰⁰ von der Crone (note 162) at 4.

answered. Even the relatively settled opinion that the abolishment of the share capital concept would entail the abandonment of the capital maintenance rule is contested in the second model.

The first model appears to be the most advanced. But on a second look it is doubtful whether it is really concerned with finding a viable proposal for the reform of Swiss company law which is still deeply anchored in the European continental law tradition of a systematically closed share capital system. It is certainly undisputed that the American Model possesses several advantages over the rigid share capital system. It cannot be denied that it is more flexible, more solution oriented and less bound to formalities. The weaknesses of the capital protection rules especially as an efficient mean of creditor protection are perceived by all relevant law authorities. But the weak point of the first model is exactly that it is restrained to an explanation of the advantages of the American Model over the share capital system without giving a clue of how the implementation of a non share capital system could in reality be carried out in Swiss Company Law. Its findings are simply that an overall assessment would show that the solution oriented approach of the American Model is to be preferred over the formalistic share capital system. But where does this conclusion lead to? Is it a hidden recommendation to simply adopt the Revised Model Business Corporation Act 'tel quel' for Swiss Company Law? This can obviously not been meant as such an abrupt change would knock out the corporate business community in Switzerland. The important question which is left unanswered in the model is therefore how to implement the advantages of a non share capital concept into a legal system with a completely different legal and social background than the American Model. On this level a lot of 'field studies' and preparation work still need to be done in order to enable the legislator to adopt in the future a comparable - but hardly identical - model as provided in the Revised Model Business Corporation Act. The first scheme gives at best new impulses for such further studies but, remains very vague as to the question how the current system should be reformed.

Furthermore, even though Switzerland is not yet part of the EU and therefore in principle not obliged to follow the guidelines of the Second Company Law Directive of 13 December 1976 it is nevertheless worth mentioning that introducing such a progressive approach would for the moment be contradictory to European Company Law. Should Switzerland join the EU at a later stage it could be necessary to readopt the share capital system. It has been vaguely argued that for the time being it could however be a competitive advantage for Switzerland to adopt a modern approach towards capital rules.²⁰¹

The second and third models on the other hand clearly indicate in their respective field of priority which way the legislature would have to go in order to realize the set objectives as there are: a modernization of capital protection rules and a more flexible capital structure. The second model abolishes the share capital concept but enforces the capital protection rules linked to the new reference size 'capital reserve'. The third model maintains the share capital concept but introduces a 'capital band' as well as 'notional no par value shares' without further regard to capital protection rules. However differently the priorities are set within these two models it is not impossible to combine them. A capital band as proposed in the third model can be introduced in a non share capital system as proposed in the second model in so far as in the articles of incorporation it is not only stated how many shares can be issued at maximum (authorized capital) but, as well how many shares can be taken back freely (i.e. without going through a formal reduction of the 'capital reserve').²⁰² The increase and reduction of the 'capital reserve' within the 'capital band' would be in the authority of the board of directors. The capital maintenance rule would therefore only apply insofar as the number of issued shares would after the reduction fall below the minimum amount specified in the articles of incorporation. However, in such a system it would be very difficult for creditors to know up to which amount the equity is exactly protected against a return to the shareholders since the market value of a share may vary from day to day.

²⁰¹ Stoffel (note 177).

²⁰² Böckli (note 184) at 733-34.

The second and third model might be realizable proposals in order to create a more flexible capital concept for Switzerland. But at the same time they are still anchored in the share capital concept with all its perceived disadvantages. The second model purports to give up the share capital concept but in fact the introduced notion 'capital reserve' is not more than an aggregation of what are presently the payments on nominal value (share capital), the premiums and legal reserves. Until now the capital maintenance rule is only targeted at the share capital and the legal reserves. Without the differentiation between share capital and premium in a non share capital system the entire issue price would become subject of the capital maintenance rule. There is no qualitative difference to a 'notional non par value share' system. Capital increases are effected of course more easily in this model but, the reason being is not the renaming of 'share capital' in 'capital reserve' but the authority of the board of directors for the issue of shares up to the authorized share capital. Such a change in competence can be effected even within a traditional share capital system. The second model on its own would bring a very modest modernization of the capital system if - as it is generally the case - modernization is understood as developing towards the American Model. Going into the opposite direction by strengthening the capital protection rules (which is in truth the substance of the second model) is in fact an alternative model which cannot claim for itself to receive much support in current international legal doctrine.

The third model is the most 'honest' in so far as it does not purport to be more of a change than it actually is. It clearly indicates how the Swiss Company Law should be adapted in order to realize the (even though modest) steps to render share capital more flexible. As opposed to the first model the realisation of the well elaborated third model within the nearer future is a realistic scenario. Of course the share capital system is preserved since the model is limited to the introduction of the 'notional no par value share'. The introduction of the 'capital band' provides more flexibility not by abolishing the share capital structure but by giving the board of directors the authority within the 'capital band' to increase and reduce the share capital and at the same time depleting the respective

procedures of some of the most burdensome formalities. The third model is by no means revolutionary if a convergence with the American Model is defined as the desirable end result of a modernization of capital structures. However, it is a realistic step in order to accustom the corporate legal community to a broadened authority of the board of directors thereby departing from the almighty principle of supremacy of the general meeting of shareholders which is still omnipresent in Swiss Company Law.

2.5. Reform steps undertaken

The most important major reform process of Swiss Company Law took place between 1968 and 1991. This is even for a country where the mills of the legislator traditionally grind slowly a record-breaking period of time.²⁰³ The first parliamentary petitions in order to revise the Company Law have already been submitted in 1957 when two members of the parliament required the introduction of shares with a smaller or even no par value in order to make it possible for a broader part of the population to acquire shares and to provide new financial funds for the increasing demand of financial means in the economy. The Federal Department of Economic Affairs (DEA) established a research group in 1959 in order to identify the need for no par value shares or at least par value shares with a smaller nominal value.²⁰⁴ The conclusion of the research group published in a special edition of the DEA monthly magazine *Volkswirtschaft* was that the introduction of 'real no par value shares' would make sense in principle but that the achieved advantages would be modest in comparison with the comprehensiveness of the law reform thereby needed. The necessity was not perceived as such to justify the otherwise indispensable initiation of a more fundamental research work on the subject.²⁰⁵ This negative approach was adopted in the following by the working committees established by the Federal Department of Justice and Police (FDJP) in order to prepare the law reform and

²⁰³ P Forstmoser 'Alter Wein in neuen Schläuchen?' (1992) 111 ZSR 1 at 3-4.

²⁰⁴ The Swiss Federal Council 'Botschaft über die Revision des Aktienrechts vom 23. Februar 1983' *BBJ* 1983 745 at 772.

²⁰⁵ Federal Department of Economic Affairs (ed) 'Kleinaktien und nennwertlose Aktien, Bericht der vom Eidg. Volkswirtschaftsdepartement eingesetzten Studiengruppe' special edition 69 of the periodical *Volkswirtschaft* (Bern: DEA, 1961) 20; von der Crone (note 162) at 3.

the subject consequently was not further investigated.²⁰⁶ The reform process was completed in 1991 and became legally effective on 1st July 1992.

The principal thrusts of this reform - as far as the concern for the present assignment - were a facilitation of capital procurement, an enforcement of the capital protection and the principal permission - under certain restrictions - of share buy backs:

- The facilitation in capital procurement was achieved by simplifying the ordinary share capital increase procedure²⁰⁷, by introducing the authorized increase of capital²⁰⁸ as well as the capital increase subject to a condition²⁰⁹ and by simplifying the financial reorganization process of a company.²¹⁰ In compliance with the recommendations of the reform commissions and despite the negative approach of the federal council of Switzerland²¹¹ the minimum par value of a share was furthermore reduced from CHF 100 to CHF 10.
- The accentuation of capital protection was realized firstly by an increase of the minimum share capital from CHF 50'000 to CHF 100'000 of which at least CHF 50'000 must be paid in on incorporation of the company. Secondly, the required formalities on raising of share capital were tightened as far as contributions in kind and acquisitions of assets were concerned through the introduction of an examination of the founders' report and an examination of the report of capital increase by an auditor (cp. Articles 635a and 652f OR). The founders report for example contains apart from others a written account for the nature and condition of contributions in kind or acquisitions of assets and the adequacy of their

²⁰⁶ The Swiss Federal Council (note 204) at 787.

²⁰⁷ The board of directors has received more authority in carrying out share capital increases upon the resolution of the general meeting of shareholders.

²⁰⁸ Cp. note 180.

²⁰⁹ According to Article 653 ff. OR the general meeting of shareholders can now decide on an increase of capital by providing in the articles of incorporation that the obligees of new bond issues or similar debt instruments of the Company as well as employees can be granted preemptive rights to new shares. The share capital is thereby increased without further action at the time and to the extent that these conversion or option rights are exercised and obligations for contributions are fulfilled by set-off or by payment.

²¹⁰ The Swiss Federal Council (note 204) at 770-71.

²¹¹ The Swiss Federal Council (note 204) at 786.

valuation. The auditor must in the following examine this report and confirm in writing its completeness and accuracy.²¹²

- Share buy backs, until then prohibited with certain exceptions, were now allowed within the following strict limits: the total par value of treasury shares may not exceed 10% of the share capital and the acquisition must be effected through freely disposable equity over the necessary amount. Furthermore an amount corresponding to the acquisition value must be allocated to legal reserves designated as reserves for own shares.²¹³

Since then the only reform worth mentioning in relation to the subject of this assignment is the further reduction of the minimum par value of a share from CHF 10 to 1 cent coming into force on 1st May 2001. The main reasons brought forward for this amendment were that a smaller par value would provide a higher liquidity of the respective shares and were more likely to attract Anglo-Saxon investors who generally are critical towards high nominal values. Additionally, problems of arithmetic nature in the course of mergers, demergers and restructuring procedures could be eliminated and stock option plans for employees facilitated.²¹⁴

2.6. Reform steps to be expected

The three major models which are currently discussed in Swiss corporate doctrine have already been discussed in section 2.3. From the official side, a reform process was initiated in the beginning of 2001. As far as the present topic is concerned the Federal Office of Justice has - based on two parliamentary petitions of the Commission for Economy and Duties in later 2000 - mandated Professor Hans Caspar von der Crone of the University of Zurich on 4 May 2001 to draw up an expert opinion concerning amongst others the question how to render capital structures in companies more flexible and whether thereby 'notional' or 'real no par value shares' should be adopted in Swiss Company

²¹² The Swiss Federal Council (note 204) at 771-72.

²¹³ The Swiss Federal Council (note 204) at 805 ff..

²¹⁴ Böckli (note 165) at 334.

Law.²¹⁵ The report of Professor von der Crone to the Federal Office was publicized in the Swiss law magazine REPRAX in 2002²¹⁶ and represents the third model as discussed in section 2.3. (c).

The draft legislation on the company law reform is written but not yet approved by the entire Federal Council of Switzerland. This decision necessary to open the consultation procedure and thereby make the draft publicly available can - according to an oral statement of the officially responsible person in the Federal Office of Justice - not be expected before December 2005. And the consultation procedure thereafter can easily again take as long as two years. The Federal Council has set itself the target to report its final comments ('Botschaft') to the revised draft by the end of the legislative period (December 2007). After that, the revised draft is still to be presented to the parliament where the discussions could again take years before an affirmative decision within both chambers²¹⁷ can be achieved.

Even though the draft legislation is not yet public one must not be too adventurous in predicting that the main features of the third model as discussed in 2.3 (c) will be a substantial part thereof. On the one hand the Federal Office of Justice has not solicited further expert reports in the field of capital structures and on the other hand no viable models are yet developed in doctrine to totally replace the share capital system in Switzerland. Therefore, the 'notional no par value share' as well as the 'capital band' can certainly be expected to be most certainly integrated in the draft legislation. The capital band will presumably consist - as delineated in the third model - of a basis capital and a maximum capital and the board of directors will receive authority to effect deliberately between these two benchmarks share capital increases and reductions by obeying thereby a simplified and accelerated procedure.²¹⁸ More advanced proposals are not to be expected and even these relatively moderate steps to

²¹⁵ Federal Office of Justice 'Aktienrechtsreform' available at <http://www.ofj.admin.ch/d/> (accessed 13 September 2005); von der Crone (note 162) at 1-2.

²¹⁶ von der Crone (note 162).

²¹⁷ The National Council and the Council of States.

²¹⁸ cp. as well press release of the Federal Office of Justice 'Einführung der nennwertlosen Aktie - Bundesrat plant Teilrevision des Aktienrechts' of 19 December 2001 available at http://www.admin.ch/cp/d/3c206f3c_1@fwsrvvg.bfi.admin.ch.html (accessed 13 September 2005).

increase the flexibility of the share capital structure will - as discussed above - still take years to become legal reality.

3. Legal situation in EU

3.1. *Capital maintenance rule*

The harmonization programme for Company Law within the EU which started in the early 1960's has been ambitious and to a great extent successful. The harmonization power of the EU is broad within the field of company law since it is generally acknowledged as an important aspect in realizing the principal goal of a common market within the EU.²¹⁹ European Company Law is mostly contained in directives, i.e. subordinate legislation which is based on the Treaties of the EU. Directives are not directly applicable but addressed to the Member States who have to implement them into their national legal order. The choice of this legal instrument enabled the Member States to compromise on common principles rather than on precise wordings which was easier, given the fact that the legislative traditions differed quite considerably within the Member States.²²⁰ Today, a largely identical body of company law has developed within the Member States and many provisions implementing directives show almost identical terms. However, it must be kept in mind that European Company Law is still not a uniform law and harmonization remains partial.²²¹ Directives offer sometimes more than one alternative to reach the desired result or leave it up to the Member States to go beyond the minimum standards set by the directives.

In the present context the Second Company Law Directive of 13 December 1976 (Second Directive), adopted under Article 54 of the EC Treaty, on coordination of safeguards in respect of the formation of public limited liability companies and the maintenance and alteration of their capital is of importance. The stated aim of the Second Directive is to deliver interested persons with information about the composition of a company's capital and to ensure a minimum standard for

²¹⁹ E Wymeersch 'Company Law in Europe and European Company Law' (April 2001) Financial Law Institute Working Paper No. 2001-06 available at <http://ssrn.com/abstract=273876> (accessed on 13 September 2005) at 3.

²²⁰ Wymeersch (note 219) at 7.

²²¹ Wymeersch (note 219) at 16.

shareholder and creditor protection. The system provided by the Second Directive in order to realise these objectives is very similar to the one governing Swiss Company Law. It adheres to the share capital concept and the thereto attached capital protection rules.

The following requirements are set by the Second Directive in respect of public companies and are to be implemented into the national company law by each member state: The statutes or another instrument of incorporation must state the subscribed capital, the nominal value of the shares subscribed or the number of shares subscribed without stating the nominal value where such shares may be issued under national law (Article 3). European legal doctrine largely agrees that this provision permits the Member States to introduce the 'notional no par value share' but not the 'real no par value share'.²²² Shares might not be issued at a price lower than their nominal value or - where there is no nominal value - their accountable par (Article 8). The minimum capital required is EURO 25'000 (Article 6). On incorporation each share must be paid up at not less than 25% of its nominal value (or accountable par) (Article 9). The subscribed capital can only consist of assets which are capable of economic assessment, but in any case not of an undertaking to perform work or supply services (Article 7).

Article 15 (a) and (c) are of distinguished interest as the capital maintenance rule is explicitly stated therein: *"Except for cases of reductions of subscribed capital, no distribution to shareholders may be made when on the closing date of the last financial year the net assets as set out in the company's annual accounts are, or following such a distribution would become, lower than the amount of the subscribed capital plus those reserves which may not be distributed under the law or the statutes"* and *"The amount of a distribution to shareholders may not exceed the amount of the profits at the end of the last financial year plus any profits brought forward and sums drawn from reserves available for this purpose, less any losses brought forward and sums placed to reserve in accordance with the law or the statutes."*

²²² von der Crone (note 162) at 9 and FN 37.

Furthermore, share buy backs may - apart from other restrictions - not exceed 10% of the subscribed capital and may not have the effect of reducing the net assets below the amount of the subscribed capital plus the non distributable reserves (Article 19). Financial assistance by a company to a third party for the purchase of its own shares is in principle prohibited (Article 23). Both increase and reduction of share capital (Article 25 and 30) must be decided by the general meeting of shareholders. As far as share capital increases are concerned the board of directors can - subject to certain conditions - at least be authorized by the general meeting of shareholders to increase the subscribed capital up to a maximum amount (fixed by national law) and within a period of maximum five years (Article 25). A capital reduction may not fall below the required minimum capital (Article 34). Creditors are entitled to obtain security for due claims upon the publication of a capital reduction (Article 32). And in the case of a serious loss of the subscribed capital a general meeting of shareholders is to be called which must consider emergency measures to be taken. The amount of a loss deemed to be 'serious' may not be set by Member States at a figure higher than half the subscribed capital (Article 17).

European Company Law and Swiss Company Law are therefore very similar as far as the share capital concept and capital protection rules are concerned. The directive discussed above was enacted nearly 30 years ago and has since then remained unchanged. However, discussions about a fundamental overhaul of capital rules have also lately started in the EU and a first - even though by no means radical - reform proposal concerning the Second Directive has already been presented by the European Commission. These short and medium term reform ambitions are the subject of the next two chapters.

3.2. Reform steps to be expected (short term)

The Commission launched in 1998 a law reform program called the Simplification of the Legislation on the Internal Market (SLIM). Within this process a Company Law Working Group issued in September 1999 a Report with recommendations on the areas in which a simplification of the First and Second Company Law

Directives could be achieved.²²³ In September 2001 the Commission set up the High Level Group of Company Law Experts ('High Level Group') which further developed the recommendations of the Working Group.²²⁴ Following an extended public consultation which it held on possible approaches towards a reform of the European capital regime the High Level Group issued a 'Report on a Modern Regulatory Framework for Company Law in Europe' ('Report')²²⁵ in which - amongst others - it supplemented the recommendations of the Working Group slightly ('SLIM-Plus'). Based thereupon the Commission has developed its proposal for a new directive aimed at the amendment of the Second Directive as a first and most urgent step within the broad-based Commission's Action Plan on Company Law and Corporate Governance launched in May 2003.²²⁶ The proposal has been discussed in Council working groups and is currently being considered by the European Parliament.

The objectives of this amendment are to facilitate capital related measures taken in public companies and thereby contribute to the efficiency and competitiveness of European business.²²⁷ Certain capital measures in reaction to market developments should be possible in a less costly and protracted manner by maintaining at the same time the similar standard of creditor and shareholder

²²³ Recommendations by the Company Law SLIM Working Group on the Simplification of the First and Second Company Law Directives, September 1999; Report from the European Commission to the European Parliament and the European Council - Results of the fourth phase of SLIM - COM(2000)56 of 4 February 2000.

²²⁴ European Commission 'Proposal for a Directive of the European Parliament and of the Council amending Council Directive 77/91/EEC, as regards the formation of public limited liability companies and the maintenance and alteration of their capital' available at http://europa.eu.int/comm/internal_market/company/docs/capital/2004-proposal/proposal_en.pdf (accessed 19 September 2005) at 5.

²²⁵ Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe, November 2002 available at http://europa.eu.int/comm/internal_market/en/company/company/modern/consult/report_en.pdf (accessed 19 September 2005) at 4.

²²⁶ Press release of the European Commission 'Company law: Commission proposes to simplify the formation, maintenance and alteration of companies' capital' of 29 October 2004 available at http://europa.eu.int/comm/internal_market/company/capital/index_en.htm (accessed on 19 September 2005).

²²⁷ European Commission 'Communication to the Council and the European Parliament: Modernising Company Law and Enhancing Corporate Governance in the European Union - A Plan to Move Forward' available at http://europa.eu.int/eur-lex/en/com/cnc/2003/com2003_0284en01.pdf (accessed on 20 September 2005) at 3, 8, 9-10.

protection.²²⁸ The proposed changes in order to reach such ambitious aims are however not of fundamental nature: the need for expert valuation of contributions in kind upon incorporation or share capital increases will be abolished in cases where there is a clear point of reference for the valuation of such consideration, financial assistance provided by a company for the acquisition of its shares by a third party will - subject to certain safeguards - be allowed up to the limit of the company's distributable reserves, the procedure of share capital increases will become less burdensome by relaxing the current rules on the limitation or withdrawal of pre-emption rights and the right for a company to acquire its own shares up to the limits of distributable reserves will be introduced.²²⁹

3.3. Reform steps to be expected (medium term)

But the Commission's Action Plan on Company Law and Corporate Governance also includes a medium-term strategy to reconsider an alternative concept to the share capital system.²³⁰ The share capital system as one of the cornerstones of European Company Law was recently openly challenged by the High Level Group: apart from supplementing the proposals of the SLIM Working Group foremost directed at rendering the Second Directive simpler and more efficient it furthermore presented two alternative models which would abandon the legal capital concept. After the implementation of such an alternative system the High Level Group is of the opinion that the Member States should be able to freely decide whether to change to this new regime or to retain the system as provided in the Second Directive.²³¹ This despite the fact that the High Level Group expressed severe criticism towards the current share capital system: the legal capital would give no indication whether the company's assets are sufficient for its entrepreneurial activity and would fall short in reaching its principal goals which are creditor and shareholder protection. Creditors would only be interested in the question whether or not a company is able to pay its debts and to answer this question the share capital would only give a very primitive and inaccurate

²²⁸ European Commission (note 224) at 2.

²²⁹ European Commission (note 224) at 7-8.

²³⁰ European Commission (note 227) at 18.

²³¹ Report High Level Group (note 225) at 80-81.

indication. The inflexibility of the current system would furthermore have a negative impact on the cost and efficiency of equity funding.²³²

These weak points of the current system have led the High Level Group to consider alternative models and to conduct an extensive consultation process within the interested European corporate community which has received a wide response. It emerged however that a radical change based on the American Model could not find much favour. A second alternative model outlined by the High Level Group which also departs from a non share capital concept but which, at the same time, retains some basic features of the European Company Law received a much more positive feedback. This model aims at integrating modern, more efficient mechanisms for creditor protection into the European style of company where the power in relation to operations concerning shareholders' equity is with the general shareholder meeting.²³³

In its Report the High Level Group delineated the major characteristics of how such a new regime could look like: A solvency test for any distributions to shareholders (including share buy-backs and capital reductions) would be introduced. The solvency test would be twofold; it would contain a balance sheet test (the assets must fully cover or exceed liabilities after the proposed distribution) and a liquidity test (the company must have sufficient liquid assets to make payments of the liabilities as they fall due in the following period, e.g. the forthcoming twelve months). Furthermore the requirement to retain a certain solvency margin on a continuing basis should be evaluated. The fulfilment of the solvency test should be explicitly confirmed by the board of directors and they would become liable for the incorrectness of such a certificate. Exclusion or limitation of pre-emption rights would in principle still only be possible, based on a resolution of the general shareholder meeting. Shares could henceforth only be issued at a fair value which necessarily would have to stand in a relation to the real value of the existing shares. The protection of shareholders would thereby normally be improved compared to the present requirement not to issue shares

²³² Report High Level Group (note 225) at 78-79.

²³³ Report High Level Group (note 225) at 80.

below par value. Shares which are issued for contributions in kind could be made subject to a respective resolution of the general shareholder meeting and directors could be required to certify the appropriateness of the consideration in the light of the fair value of the existing shares.²³⁴

The model presented by the High Level Group is not yet fully fledged and needs some further refinement. A public consultation on the Commission Action Plan has in fact shown that a further study into the feasibility of an alternative to the share capital system is largely welcomed. But round about half of the respondents have harshly criticized the possible introduction of an alternative regime: such a radical change of system even at a later stage would result in a loss of transparency and creditor protection. Furthermore, the alternative introduction of a completely different concept would endanger the harmonisation so far achieved within the EU and introduce an unwelcome division of law.²³⁵

The Commission has however called for tenders until 26 September 2005 to draw up a feasibility study concerning alternatives to the current share capital regime.²³⁶ The study should evaluate whether within an alternative regime an equal standard of creditor and shareholder protection could be achieved by enhancing at the same time efficiency and competitiveness of business. The final report is expected at the end of 2006.

3.4. *Excursus: Legal situation in GB*

In the context of the present assignment the position of Great Britain is of particular interest. On the one hand Great Britain is a member of the EU and therefore subject to the limitations set by the legislation of the EU. On the other hand it is a common law country where company law is guided by completely

²³⁴ Report High Level Group (note 225) at 86-89.

²³⁵ DG Internal Market 'Synthesis of the responses to the Communication of the Commission to the Council and the European Parliament: Modernising Company Law and Enhancing Corporate Governance in the European Union - A Plan to Move Forward' available at http://europa.eu.int/comm/internal_market/en/company/company/modern/governance-consult-responses_en.pdf (accessed 21 September 2005) at 19.

²³⁶ Call for tender MARKT/2005/13/F 'Feasibility study on alternative to capital maintenance regime as established by the Second Company Law Directive 77/91/EEC of 13.12.1976 and the examination of the implications of the new EU-accounting regime on profit distribution' available at http://europa.eu.int/comm/dgs/internal_market/calls_en.htm (accessed 21 September 2005).

different principles and traditions than that of the major part of other member countries. Together with Ireland, Great Britain forms a small minority of common law nations within the EU what is highly unfortunate within any decision-making body.²³⁷ Reform in Great Britain as far as company law is concerned had in the past four decades mainly been limited to the implementation of EC directives. Unlike in most of the other common law countries the capital maintenance rule was even strengthened in English company law.²³⁸ A harmonization with continental law systems has taken place and consequently an alienation from other common law systems. Other common law countries like Australia, New Zealand, Canada and South Africa who once looked to Great Britain to lead the way have already modernized their law in the course of the revised American Model Business Corporation Act. It is therefore not surprising that the English influence on common law has decreased considerably within Company Law in the past three decades.²³⁹ Critical voices within the country considered this assimilation of continental company law principles as contradictory to the business needs and commercial values as they have materialized in recent years.²⁴⁰ Great Britain should be more vigilant henceforth to use all its possible influence within the EU to shape the terms of the future agenda according to their comprehension of modern business needs instead of trying to influence detailed proposals once the program has already been made.²⁴¹

The need for a fundamental review of the British company law was strongly perceived within the British corporate community and the Department of Trade and Industry (DTI) has in reaction thereto launched a long-term program in March 1998 with the aim *“to develop a simple, modern, efficient and cost*

²³⁷ LS Sealy *Company Law and Commercial Reality* (London: Sweet & Maxwell, 1984) 83.

²³⁸ JT Pretorius/PA Delpoit/M Havenga/M Vermaas *Hahlo's South African Company Law through cases* 5ed (Cape Town: Juta & Co., 1991) 170.

²³⁹ BL Welling *Corporate Law in Canada - the Governing Principles* 2ed (Toronto: Butterworths, 1991) 38.

²⁴⁰ Sealy (note 237) at 75.

²⁴¹ Sealy (note 237) at 82-84; Department of Trade and Industry 'Promoting Competitiveness: The UK approach to EU company law and corporate governance' available at <http://www.non-exec-register.com/frame/?title=&url=%2Fpdf%2FUKApproachToEUCompanyLaw%2Epdf> (accessed 22 September 2005) at 5.

effective framework for carrying out business activity in Britain²⁴² The Company Law Review was led by an independent Steering Group consisting of persons with particular knowledge and expertise in company law matters. The Final Report was presented to the Secretary of State in 2001.²⁴³ In March 2005 the Government published a White Paper²⁴⁴ in which most of the recommendations of the Final Report were included. The White Paper was subject to consultation until 10 June 2005. Currently the responses are being evaluated.²⁴⁵ The reforms will be introduced through the Company Law Reform Bill as soon as Parliamentary time allows.²⁴⁶

A key issue of the reform was the deregulation of the capital maintenance regime. As far as public companies are concerned the reform ambitions were constrained by the Second Directive.²⁴⁷ The fact that the Second Directive does indirectly prohibit the introduction of 'real no par value shares' and does only in very limited cases allow the provision of financial assistance by a company for the acquisition of its own shares by a third party was perceived as especially burdensome.²⁴⁸ Consequently the deregulation will predominantly (but not only) take place in respect of private companies which are not subject of the Second Directive. The planned relaxation of the capital maintenance rule includes the following measures: abolishing the restrictions on financial assistance for the acquisition of a company's own shares in respect of private companies, the elimination of authorized share capital (no ceiling must be included anymore in companies' constitutions of the number of shares which might be issued) and reserve capital, the application of the share premium account will be limited, private companies can carry out capital reductions by a solvency statement of

²⁴² Department of Trade and Industry 'Corporate Law and Governance Subject: Company Law Reform' available at <http://www.dti.gov.uk/cld/review.htm> (accessed 22 September 2005).

²⁴³ Company Law Review Steering Group 'Modern Company Law for a Competitive Economy: Final Report' available at http://www.dti.gov.uk/cld/final_report/anx_b.pdf (accessed 22 September 2005).

²⁴⁴ Department of Trade and Industry 'Company Law Reform White Paper' available at <http://www.dti.gov.uk/cld/WhitePaper.htm> (accessed 22 September 2005).

²⁴⁵ Department of Trade and Industry (note 242).

²⁴⁶ Department of Trade and Industry 'Company Law Reform White Paper: Frequently Asked Questions' available at <http://www.dti.gov.uk/cld/doc31.doc> (accessed 22 September 2005).

²⁴⁷ Department of Trade and Industry (note 241) at 10.

²⁴⁸ Company Law Review Steering Group (note 243) at 337-338.

the directors instead of a Court order, private companies are dispensed from shareholder authorization to allot shares provided that after the issue the company will have not more than one class of shares and finally no authorization for capital reductions or share buy-backs are required anymore in the articles of companies.²⁴⁹

Given the constraints which Great Britain was confronted within its reform program it is not surprising that the current reform ambitions of the EU, especially the Action Plan of the Commission, are very much welcome.²⁵⁰ Depending on the outcome of the feasibility study currently in progress, an alternative to the current capital maintenance regime does not seem out of reach anymore. The DTI has furthermore taken seriously the above mentioned criticism to mark its presence earlier and tries to involve British stakeholders in the development of the Action plan with the recent publication *Promoting Competitiveness: the UK approach to EU company law and corporate governance*.²⁵¹ This booklet is a serious attempt to motivate the British corporate community to take actively part in the process of lobbying not only with the EU institutions but, also with the relevant Committees, decision makers and business organizations in other Member States. Great Britain has accepted that what the EU does on company law is not only of fundamental importance for UK companies and investors but above all for its own scope for reform.

4. South Africa: a role model for Switzerland?

As discussed in the first part of this assignment South Africa has largely given up the capital maintenance rule by retaining at the same time the share capital concept. It has been criticized that the Companies Amendment Act of 1999 shows a lack of consequence as not every provision upholding or derived from the capital maintenance rule has been properly adapted to the new concept 'solvency and liquidity test'. It has been further argued that the share capital

²⁴⁹ Department of Trade and Industry 'Share capital: Explanatory material' available at <http://www.dti.gov.uk/cld/doc17.doc> (accessed 22 September 2005).

²⁵⁰ Department of Trade and Industry (note 244) at 9; Department of Trade and Industry (note 241) at 4.

²⁵¹ Department of Trade and Industry (note 241) at 10.

concept might as well been given up by the Companies Amendment Act 1999 since the residual meaning of the capital accounts is now - if anything - very restricted. The share capital has forfeited its former function as reference size for the capital protection provisions and stands now as a rather awkward shell in the revised Companies Act 1973. The overall impression one gets from the actual version of the Companies Act is not that South Africa chose deliberately a middle way but, that the result is rather a consequence of the hastened and deficient reform process. The stated aim of the reform process which is currently taking place in South Africa is therefore foremost to do away with these insufficiencies. The result which can be expected will most certainly rely heavily on the American Model. But for the time being, the question whether South African Company Law (in its present status) could serve as a role model for Swiss Company Law must - due to the inconsistent conversion into the chosen model - be answered in the negative.

After the current reform process will be completed in South Africa the question might as well be reformulated in whether the American Model could serve as well as a role model for Swiss Company Law. In Switzerland as well as in the EU the current reform ambitions to relax the capital maintenance rule are indeed clearly influenced by the perceived advantages which are anchored in the non share capital system as developed by the American Model. But both in Switzerland as well as in the EU skepticism is still discernible when it comes to the ultimate question whether the capital maintenance regime should be totally abolished. As shown above, the share capital concept as a coherent and close system is still partly perceived as affording a minimal creditor and shareholder protection. An alternative regime would only have a chance if it is assured that it guarantees at least an equal standard of such safeguards. Concerns of this nature are addressed completely different and to a lesser degree normative within the American Model where creditors as well as minority shareholders are in principle expected to provide for their own protection through negotiated agreements. Even though the major part of the Continental European legal community perceives the same weaknesses of the current share capital system the

proposed solutions vary considerably when it comes to the question how these weaknesses should be overcome. An alternative model which would allow replacing more or less smoothly the current share capital system in Continental Europe seems not yet operational, wherefore the EU is about to commission a respective feasibility study. For Switzerland it is at the moment certainly rational and cost-effective to wait for the outcome of this feasibility study before taking into consideration a major departure from the existing harmony. This even more so as Switzerland has approached the EU in the last years significantly through bilateral agreements and a later joining as a full member state is not excluded. From a middle to long term perspective, the share capital system in Europe will not only be rendered more flexible but most certainly replaced by a new concept. Such a concept will by all means be inspired by the advantages of the American Model. A plain adoption of the American Model in the EU or in Switzerland is however unrealistic and a convergence of the two systems is restricted since a European concept - to be acceptable to a majority - will in principle still have to provide for the supremacy of the general shareholder meeting over the board of directors.

5. Revised Model Business Corporation Act: a role model for South Africa?

The progression of the current reform ambitions in South Africa leaves no doubt about this question: Members of the American Bar Association have been closely involved in the reform process from the start and the recommendations of their Report in respect of the capital structure have been integrated in the Guidelines almost verbatim.²⁵² Of course there is some further consultation planned but it seems very likely that the end result as far as capital rules are concerned will be based upon the American Model. Already the Companies Amendment Act 1999 has - at least indirectly - been inspired by the American Model in so far as it borrowed heavily from the Canada Business Corporations Act 1985 which on its part is influenced by the American predecessor. The approach in the current

²⁵² cp. section 1.6..

reform procedure is therefore not new; it is aimed to complete and harmonize the Companies Act in conformance with the underlying paradigm shift induced already by the Companies Amendment Act in 1999.

The heavy influence of the recommendations of the American Bar Association on the Guidelines has not, of course, remained unnoticed and has been criticized as problematic during the current consultation process.²⁵³ It has been held that the focus would be wrongly chosen if the need to bring South African Company Law in line with international trends would take precedence over the requirement to adapt the new legislation to *“the legal, economic and social context of South Africa”*.²⁵⁴ Values which are special in the context of South Africa like the need for social sustainability would be neglected by putting too strong an emphasis on efficiency.²⁵⁵

These reflections are certainly justified as general remarks and there would have certainly been more diplomatic ways to implement the recommendations of the American Bar Association than to more or less copy them into the Guidelines. But as far as capital rules are concerned such criticism lacks tangible substance since the choice of a capital concept is a highly technical and largely non-political question. Capital rules are simply not suitable to integrate social value considerations in the sense like the new Constitution of South Africa upholds them. The capital concept in the Companies Act, especially the abolishment of the capital maintenance rule, needs undoubtedly further refinement and perfection which has in essentially the same terms been brought forward by South African law authorities even before the American Bar Association was involved.²⁵⁶ There are not so many different ways to achieve these aims and it seems not altogether unreasonable to attach a special value to reflections expressed by persons who are most familiar with the ultimate source of the model chosen by South Africa.

²⁵³ Congress of South African Trade Unions ‘COSATU input: Guidelines for Corporate Law Reform’ available at <http://www.cosatu.org.za/docs/2004/reform.pdf> (accessed 27 September 2005) at 11.

²⁵⁴ Congress of South African Trade Unions (note 253) at 4.

²⁵⁵ Congress of South African Trade Unions (note 253) at 4.

²⁵⁶ Cp. as well section 1.5. above.

6. Summary

The tendency in all of the three discussed company law systems (South Africa, Switzerland, European Union) is manifest: the share capital structure will be rendered more flexible in short term and is likely to be abolished in the middle to long run. The development in all three countries is thereby influenced by the perceived advantages of the American Model even though to a different degree: Where in the EU as well as in Switzerland scepticism can still be perceived towards a non share capital system in which creditor and shareholder protection would not anymore be linked to a bar figure South Africa is currently considering to converge further with the American Model not only in respect of the consistent application of the solvency and liquidity test - replacing thereby the capital maintenance rule - but as well in respect of the complete abolishment of the par value and stated capital concept.

In Switzerland it can be expected that the current reform process will bring a certain relaxation of the share capital rules as well as a slight decrease of the supremacy of the general shareholder meeting with the introduction of the capital band. Furthermore, 'notional no par value shares' will most certainly be introduced. Before taking off to more adventurous reform steps Switzerland will carefully watch the developments in the EU, especially the outcome of the feasibility study in respect of alternatives to the share capital regime.

The EU will according to the Commission's Action Plan on Company Law and Corporate Governance modernize its Second Company Law Directive. The proposals in order to facilitate capital related measures in companies are thereby still relatively modest but can be expected to materialize in short term. A more resolute step, the abolishment of the share capital concept, is currently subject of a feasibility study. The introduction of an alternative capital concept is strongly lobbied by Great Britain as one of the two only common law countries within the EU.

However different the opinions in relation to an alternative capital concept in the examined jurisdictions might be, on one point seems to be agreement: the prototype of the continental European share capital system is outdated. Its

stringent formalism and comprehensiveness has become an end in itself without serving its original purpose of shareholder and creditor protection sufficiently. Whichever way chosen to reform the capital concepts the pursued objective will be identical: capital measures in reaction to market developments must be possible in a less costly and in a swifter manner in order to contribute to the efficiency and competitiveness of business by maintaining at the same time sufficient safeguards for shareholder and creditor interests.

C Table of Abbreviations

BBI	Bundesblatt
BEE	Black Economic Empowerment
Bond LR	Bond Law Review
COSATU	Congress of South African Trade Unions
CRIC	Coordinating Research Institute for Corporate Law
DEA	Department of Economic Affairs
DG	Directorate General
DTI	Department of Trade and Industry
EC	European Community
EEC	European Economic Community
EU	European Union
FDJP	Federal Department of Justice and Police
H.M.S.O.	Her Majesty's Stationery Office
JSE	JSE Securities Exchange South Africa
LAWSA	The Law of South Africa
NZZ	Neue Zürcher Zeitung
OR	Swiss Code of Obligations
Reprax	Zeitschrift zur Rechtsetzung und Praxis im Gesellschafts- und Handelsregisterrecht
SA Merc	South African Mercantile Law Journal
SAC	Standing Advisory Committee on Company Law
SACRO	South African Companies Registration Office
SALJ	South African Law Journal
SJZ	Schweizerische Juristen-Zeitung
SLIM	Simpler Legislation for the Internal Market
TSAR	Tydskrif vir Suid-Afrikaanse Reg
UK	United Kingdom
UOFS	University of the Free State
ZBJV	Zeitschrift des bernischen Juristen-Vereins
ZSR	Zeitschrift für Schweizerisches Recht

D Bibliography

South African Part

American Bar Association Section of Business Law Committee on Corporate Laws 'Report on South African Companies Act No. 61 of 1973 and Related Legislation' available at www.sn.apc.org/usaidsa/usaidsa/corporate.pdf (accessed 28 July 2005).

J Armour 'Share Capital and Creditor Protection: Efficient Rules for a Modern Company Law?' (2000) 63 *MLR* 355 365.

RC Beuthin / SM Luiz Beuthin's *Basic Company Law* 2ed (1992) Durban: Butterworths.

MS Blackman/ RD Jooste/ GK Everingham *Commentary on the Companies Act* Volume 1 (2002) Wynberg: Juta and Company.

MS Blackman 'Companies' *LAWSA* vol 4, Part 1 First Reissue (1997) Durban: Butterworths.

Board of Trade, Company Law Committee *Report of the Company Law Committee (Jenkins Report) 1961-62* (1962) London: H.M.S.O.

FHI Cassim 'The New Statutory Provisions On Company Share Repurchases: A Critical Analysis' (1999) 116 *SALJ* 760.

HS Cilliers et al *Corporate Law* 3ed (2000) Durban: Lexisnexis Butterworths.

RC Clark *Corporate Law* (1986) Boston Toronto: Little, Brown and Company.

Committee on Corporate Laws 'Changes in the Model Business Corporation Act - Amendments to Financial Provisions' (1979) 34 *Bus. Law.* 1867.

Congress of South African Trade Unions 'COSATU input: Guidelines for Corporate Law Reform' available at <http://www.cosatu.org.za/docs/2004/reform.pdf> (accessed 27 September 2005).

PA Delport 'Capital Rules in South African Company Law' in JJ Henning/PA Delport/MM Katz (eds) *The Future Development of South African Corporate Law* (1994) Bloemfontein: University of the Orange Free State Coordinating Research Institute for Corporate Law 133.

Deneys Reitz Attorneys 'Section 38 - Let it BEE?' Commercial Update No 12 available at <http://www.deneysreitz.co.za/publications/pdf/Commercial%20Update%20No.12.pdf> (accessed 20 July 2005).

Department of Trade and Industry 'South African Company Law for the 21st Century Guidelines for Corporate Law Reform' (May 2004) available at https://www.saica.co.za/documents/Draft_policy_document_on_Corporate_Law_Reform.pdf (accessed 27 July 2005).

Department of Trade and Industry, Companies and Close Corporations Registration Office 'Proposals in respect of the purchase by a company of its own shares' (1992) Pretoria.

RWV Dickerson/JL Howard/L Getz *Proposals for a New Business Corporations Law for Canada* (1971) Ottawa: Information Canada.

JJ Du Plessis 'Enkele Internasionale Maatskappyregtelike Ontwikkelings' (1992) *TSAR* 561.

JSE Fourie 'South African Corporate Law Reform - Lessons from abroad' in JJ Henning/PA Delpoit/MM Katz (eds) *Selected Essays on South African Entrepreneurial Law* (1996) Bloemfontein: University of the Orange Free State Coordinating Research Institute for Corporate Law 62.

LCB Gower *Principles of Modern Company Law* 4ed (1979) London: Stevens & Sons.

LCB Gower *Principles of Modern Company Law* 3ed (1969) London: Stevens & Sons.

Great Britain Company Law Amendment Committee *Greene Report 1925-26* (1926) London: H.M.S.O.

HR Hahlo/E Kahn *The South African Legal System and its Background* (1968) Cape Town: Juta.

JPG Lessing 'Company-law Reform in New Zealand' (1990) 2 *SA Merc LJ* 49.

B McCabe 'The Desirability of a Share Buy-Back Power' (1991) 3 *Bond LR* 115.

JT Pretorius 'Capital maintenance doctrine in South African Corporate law' available at www.accaglobal.com/publications/studentaccountant/36856 (accessed 22 March 2005).

JT Pretorius/PA Delpoit/M Havenga/M Vermaas *Hahlo's South African Company Law through cases* 6ed (1999) Kenwyn, South Africa: Juta & Co..

JT Pretorius/PA Delpoit/M Havenga/M Vermaas *Hahlo's South African Company Law through cases* 5ed (1991) Cape Town: Juta & Co..

LS Sealy *Company Law and Commercial Reality* (1984) London: Sweet & Maxwell.

LS Sealy 'Corporate Law Reform: The Commonwealth Experience' in JJ Henning/PA Delpoit/MM Katz (eds) *The Future Development of South African Corporate Law* (1994) Bloemfontein: University of the Orange Free State Coordinating Research Institute for Corporate Law 1.

Simplification Task Force Attorney-General's Department Barton ACT 2600 'Corporations Law Simplification Program Share Capital Rules Proposal for Simplification' available at http://www.takeovers.gov.au/content/743/download/share_capital_rules_november_1994.pdf (accessed 20 October 2005).

A Trichardt/E Brincker 'Future Development of South African Corporate Law - Capital in Company Law' in JJ Henning/PA Delpont/MM Katz (eds) *The Future Development of South African Corporate Law* (1994) Bloemfontein: University of the Orange Free State Coordinating Research Institute for Corporate Law 141.

A Trichardt/K Organ/J Cilliers 'The Purchase by a Company of its Own Shares' 10 *Transactions of the Centre for Business Law UOFS* (1989).

Swiss Part

C Baudenbacher in H Honsell/P Vogt Nedim/R Watter (eds) *Basler Kommentar zum Schweizerischen Privatrecht, Obligationenrecht II, Art. 530–1186 OR* 2ed (2002) Basel Genf München: Helbing & Lichtenhahn.

P Böckli 'Nennwertlose Aktien und Kapitalschutz' in RJ Schweizer/H Burkert /U Gasser (eds) *Festschrift für Jean Nicolas Druey* (2002) Zürich Basel Genf: Schulthess 331.

P Böckli 'Revisionsfelder im Aktienrecht und Corporate Governance' (2002) 138 *ZBJV* 709.

P Böckli *Schweizer Aktienrecht* 3ed (2004) Zürich Basel Genf: Schulthess Juristische Medien AG.

R von Büren/WA Stoffel/K Schnyder/C Christen-Westenberg *Aktienrecht* (2000) Zürich: Schulthess.

HC von der Crone 'Bericht zu einer Teilrevision des Aktienrechts: nennwertlose Aktien' (2002) 1 *Reprax* 1.

Federal Department of Economic Affairs (ed) 'Kleinaktien und nennwertlose Aktien, Bericht der vom Eidg. Volkswirtschaftsdepartement eingesetzten Studiengruppe' special edition 69 of the periodical *Volkswirtschaft* (1961) Bern: DEA.

Federal Office of Justice 'Aktienrechtsreform' available at <http://www.ofj.admin.ch/d/> (accessed 13 September 2005).

P Forstmoser 'Alter Wein in neuen Schläuchen?' (1992) 111 *ZSR* 1 at 3-4.

P Forstmoser/A Meier-Hayoz/P Nobel *Schweizerisches Aktienrecht* (1996) Bern: Verlag Stämpfli+Cie AG.

T Guhl/A Kummer/JN Druey *Das Schweizerische Obligationenrecht* 8ed (1995) Zürich: Schulthess Polygraphischer Verlag AG.

WA Stoffel 'Abschaffung des Nennkapitalsystems im schweizerischen Aktienrecht?' (2001) 23 *SJZ* 533.

WA Stoffel 'Nennwertlose Aktien für die Schweiz? Plädoyer für eine Reform des Aktienrechts' *NZZ* 19/20 May 2001 at 29.

The Swiss Federal Council 'Botschaft über die Revision des Aktienrechts vom 23. Februar 1983' *BBJ* (1983) 745.

EU Part

Recommendations by the Company Law SLIM Working Group on the Simplification of the First and Second Company Law Directives, September 1999.

DG Internal Market 'Synthesis of the responses to the Communication of the Commission to the Council and the European Parliament: Modernising Company Law and Enhancing Corporate Governance in the European Union - A Plan to Move Forward' available at http://europa.eu.int/comm/internal_market/en/company/company/modern/governance-consult-responses_en.pdf (accessed 21 September 2005)

European Commission 'Communication to the Council and the European Parliament: Modernising Company Law and Enhancing Corporate Governance in the European Union - A Plan to Move Forward' available at http://europa.eu.int/eur-lex/en/com/cnc/2003/com2003_0284en01.pdf (accessed on 20 September 2005).

European Commission 'Proposal for a Directive of the European Parliament and of the Council amending Council Directive 77/91/EEC, as regards the formation of public limited liability companies and the maintenance and alteration of their capital' available at http://europa.eu.int/comm/internal_market/company/docs/capital/2004-proposal/proposal_en.pdf (accessed 19 September 2005).

Report from the European Commission to the European Parliament and the European Council - Results of the fourth phase of SLIM - COM(2000)56, February 2000.

Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe, November 2002 available at http://europa.eu.int/comm/internal_market/en/company/company/modern/consult/report_en.pdf (accessed 19 September 2005).

E Wymeersch 'Company Law in Europe and European Company Law' (April 2001) Financial Law Institute Working Paper No. 2001-06 available at <http://ssrn.com/abstract=273876> (accessed on 13 September 2005).

UK Part

Company Law Review Steering Group 'Modern Company Law for a Competitive Economy: Final Report' available at http://www.dti.gov.uk/cld/final_report/anx_b.pdf (accessed 22 September 2005).

Department of Trade and Industry:

'Company Law Reform White Paper' available at <http://www.dti.gov.uk/cld/WhitePaper.htm> (accessed 22 September 2005).

'Company Law Reform White Paper: Frequently Asked Questions' available at <http://www.dti.gov.uk/cld/doc31.doc> (accessed 22 September 2005).

'Corporate Law and Governance Subject: Company Law Reform' available at <http://www.dti.gov.uk/cld/review.htm> (accessed 22 September 2005).

'Promoting Competitiveness: The UK approach to EU company law and corporate governance' available at <http://www.non-exec-register.com/frame/?title=&url=%2Fpdf%2FUKapproachToEUCompanyLaw%2Epdf> (accessed 22 September 2005).

'Share capital: Explanatory material' available at <http://www.dti.gov.uk/cld/doc17.doc> (accessed 22 September 2005).

BL **Welling** *Corporate Law in Canada - the Governing Principles* 2ed (1991) Toronto: Butterworths.